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Politics this week

Apr 3rd 2003
From The Economist print edition

Belly of the beast

AP

American troops massed around Iraq's capital moved **closer to Baghdad**. Missiles and bombs struck military and government targets, and American forces attacked Republican Guard troops in defensive positions around the city. Heavy fighting was reported at Karbala, some 70 miles from Baghdad and coalition troops pushed across the Tigris river farther east.

See article: At the gates of Baghdad

British and American troops **fought street by street** for control of key towns and cities in southern Iraq and along the extended supply line to troops surrounding Baghdad. British troops took control of territory around Basra but faced resistance from guerrilla units within Iraq's second city.

See article: Trying to win hearts and minds in southern Iraq

Four American soldiers were killed by a **suicide bomber**. Iraq claimed that fighters and suicide bombers were arriving steadily from surrounding Arab countries. The Pentagon apologised for the deaths of seven Iraqi women and children, shot in a vehicle that failed to stop at a checkpoint. Iraq claimed heavy civilian casualties; coalition fatalities so far number less than 80.

See article: Punching through to Baghdad

Mr Hussein called for a ***jihad*** against coalition forces in a speech read out on television by his information minister. His failure to appear in person excited more speculation that he might be dead or wounded.

In the north, **Kurdish** *peshmerga* fighters, supported by American special forces, captured the stronghold of an extremist Islamist group which America has accused of having links with terrorism and al-Qaeda.

See article: Kurds and Americans rout out extremists

America's secretary of state, **Colin Powell**, visited Turkey to ask for more help with military operations in northern Iraq and to dissuade Turkey from sending troops into Kurd-held territory.

See article: Talking Turkey

A frenzy of finger-pointing broke out in Washington, as Donald Rumsfeld, America's defence secretary, had to fend off criticism from some American officers in Iraq, and **armchair generals** at home, for meddling in the army's war plan for Iraq and not sending enough troops. Mr Rumsfeld retorted that General Tommy Franks, the commander in the region, had been given everything he asked for.

See article: Those awkward hearts and minds

SARS scare

EPA

The number of people killed by SARS, a pneumonia-like virus that has spread

throughout the world from **China**, rose to 78. The places most affected were China, with 46 reported deaths, and Hong Kong, with 16.

See article: A worry the world over

Bombers again struck the southern **Philippines** city of Davao, killing 16 people at a ferry terminal. Soon afterwards, three mosques were hit by bomb attacks, perhaps in retaliation. Last month, 22 people died in a bomb attack at Davao airport. No group claimed responsibility for the attacks.

Three **Afghanistan** government soldiers were killed in a clash with rebels, believed to be Taliban, near Spin Boldak, in the south-west of the country. Afghan officials said that there had been increased Taliban activity since the start of the war in Iraq.

Indian troops shot dead the deputy leader of **Kashmir's** main militant group, Hizb-ul-Mujahideen.

South Korea agreed to send about 700 medical and other non-combat personnel to support coalition forces in Iraq. President Roh Moo-hyun said South Korea's interest lay in maintaining close ties with the United States.

Leslie Cheung, aged 46, star of “Farewell My Concubine” and other acclaimed films, jumped to his death from a hotel window in **Hong Kong**.

In the affirmative?

The Supreme Court heard oral arguments in its two most contentious cases this year. These concern **affirmative action**, the advantage which most of the nation's top universities give to aspiring African-American and Hispanic students. The court is expected to rule by the end of June on whether these preferences are constitutional.

See article: The Supreme Court and racial preferences

Free banking

Brazil's Congress voted for a constitutional amendment paving the way for central-bank independence. President Luiz Inácio Lula da Silva said he would send all-important pension and tax reforms to the Congress this month.

See article: Trying to reform Brazil

The president of **Chile's** central bank resigned, after his secretary was found to have passed information to a corrupt financial firm.

See article: Another Chilean fraud

A mudslide which enveloped a gold-prospecting town in northern **Bolivia** killed 17 people and left 200 missing.

A Cuban carrying hand-grenades **hijacked** a plane on a domestic flight and forced the pilot to fly to Florida. A day later, several armed Cubans seized a Havana ferryboat with more than 50 passengers and sailed it towards the United States.

Buggins's term

Heads of government of seven smaller **European Union** countries jointly declared their opposition to proposals by large ones for a long-lasting EU presidency in place of the present six-monthly rotating one.

For the first time, a force under the aegis of the EU undertook a **peacekeeping** role. The 300-plus

troops, under the overall command of a German admiral, have replaced a NATO-led force monitoring peace in Macedonia.

See article: The European Union goes military

The body of a former **Serbian** president, Ivan Stambolic, who disappeared while jogging in 2000, was found near Belgrade. It is suspected that he was killed by a special police unit answering to Serbia's former strongman, Slobodan Milosevic.

In a state election in **Lower Austria**, the far-right Freedom Party took only 4% of the vote, a quarter of its previous share. The conservative People's Party, which at national level heads a coalition with the Freedomites, took 50%.

Calm in Congo

EPA

Congo's government, rebel groups and opposition factions signed a pact aimed at ending the country's civil war, adopting a new constitution and paving the way for elections. But continued fighting in eastern Congo threatened to undermine the deal.

The president of **Malawi**, Bakili Muluzi, who had been seeking to change the constitution to allow himself a third term in office, relented, named a successor, and sacked his cabinet.

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Business this week

Apr 3rd 2003
From The Economist print edition

The long run

Stockmarkets were jittery over prospects of a lengthy war in Iraq, as the coalition advance into Iraq appeared to slow down after running into stiffer opposition than many had expected. News that an assault on Baghdad had begun then caused markets to rally and the oil price to fall.

Air turbulence

American Airlines avoided the immediate prospect of Chapter 11 bankruptcy protection by agreeing a tentative wage-cut with unions. The world's biggest carrier, suffering the effects of a gloomy economy, compounded by the impact of war in Iraq, will cut its wage bill for pilots, flight attendants and mechanics by $1.8 billion a year. Its shares rose sharply.

US Airways added to the (muted) cheer. America's seventh-largest airline emerged from Chapter 11 bankruptcy after over seven months. It slashed costs, capacity and jobs, saying it was “drowning but closer to the surface”.

KLM Royal Dutch was more troubled. It will make heavy job cuts, after announcing cost-cutting measures to counter the precarious state of the world economy and the twin setbacks of the Iraq conflict and the outbreak of the SARS epidemic in East Asia.

Shares in **Japan Airlines System** and **All Nippon Airways**, the country's two biggest airlines, were hit as travellers cancelled flights for fear of the SARS virus. **Singapore Airlines** shaved capacity by 4%.

See article: Crisis in corporate travel

Air Canada succumbed to the ills of the airline industry and filed for bankruptcy protection after it had failed to agree on a programme of cost cuts with key unions.

In your debt

The IMF's planned sovereign-debt restructuring mechanism—dubbed a “**sovereign Chapter 11**”—looks set for the scrap-heap after America prepared to block the proposal. The SDRM would have allowed countries in economic turmoil to suspend debt repayments; America prefers a system of “collective action” clauses attached to sovereign bonds to make it easier to reach agreement with private creditors in the event of default.

Trade negotiators missed a deadline for agreeing to cuts in agricultural tariffs and subsidies, threatening progress in the **Doha round** of trade talks.

See article: Doha in danger

Unfraternal Liberty

Liberty Media accompanied its interest in **Vivendi Universal's** American cable assets with a lawsuit alleging that the French media firm had been less than forthcoming about its financial health. The American media giant got a big tranche of Vivendi's shares in December 2001 for its stake in USA Networks; the shares subsequently tanked.

AOL Time Warner faces a further restatement of advertising revenues at its America Online division, after a restatement of $190m last year, according to regulators probing the media giant. The continuing investigation could hamper an offering of the company's cable-TV assets, delaying a reduction in its burgeoning debt pile.

The Italian telephone-directory business of **Seat Pagine Gialle** was the target for three consortiums comprising some of the world's leading private-equity firms. At a price of around *euro*4.5 billion ($4.9 billion), it would be Europe's biggest leveraged buy-out.

Blackstone, a big American private-equity group, took on David Verey as a senior adviser to beef up its European operations. Mr Verey left the role of deputy chairman of Cazenove, an upper-crust British broker, last year.

SBC Communications admitted defeat in its attempt to snatch **DirecTV**, an American satellite-TV company, from under the nose of Rupert Murdoch. The American telecoms firm failed to reach an agreement with General Motors, DirecTV's owner, allowing Mr Murdoch's News Corp a clear run at the American broadcaster.

See article: American TV's surprising travails abroad

Corus off tune

Corus was said to be in talks with **LNM**, owned by Lakshmi Mittal, a controversial Indian steel magnate, that could see the rusting Anglo-Dutch firm sell some prime assets. The news coincided with details of a new bonus scheme that would reward top managers for meeting “personal goals” rather than just (non-existent) profits.

Rumours of a takeover boosted shares of **Alstom** by 20%, but the mystery bid, which arrived on April 1st, was dismissed. Its “seriousness appeared doubtful” said the beleaguered French engineering group.

Lloyd's of London made a profit for the first time in six years. The world's oldest (and biggest) insurance market made £834m ($1.3 billion) in 2002, after losing £3.1 billion the year before.

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The War in Iraq

At the gates of Baghdad

Apr 3rd 2003
From The Economist print edition

Even a very polite victory over a reviled dictator will end up humiliating the Arabs

Getty images

Get article background

IN THE second week, the cry from the armchair generals was that the war was failing because the plan was wrong. As it entered its third, the cry from the armchair historians has been that the Anglo-American invasion of Iraq is lighting a fuse that will ignite Arab nationalism and blow up the Middle East. Both lines of criticism are wildly exaggerated, and may soon turn out to be completely wrong. But they are connected. A fast war—and this looks increasingly like being a fast war—will cause much less grief to the Arabs than a prolonged one.

This war is unpopular with Muslims almost everywhere. If Saddam Hussein really could suck the Americans and British into the Vietnam-like “quagmire” his spokesmen have promised, this would undoubtedly poison America's and Britain's relations with both the Arabs and the wider Islamic world. The suicide-bombing at an American checkpoint on March 29th, followed by the shooting by Americans of civilians at another checkpoint, provoked comparisons with the quagmire Israel has sunk into in the occupied Palestinian territories. The stream of *fatwas* declaring holy war against the invaders, and the trickle of Arab volunteers entering Iraq to fight the Americans, have provoked comparisons with the Soviet invasion of Afghanistan, which radicalised a generation of Islamists, including Osama bin Laden. The defect of these comparisons is that Iraq is nothing like Vietnam, not much like Palestine or Afghanistan, and, on present evidence, no quagmire.

A little light number-crunching

In Vietnam the Americans fought for ten years. The Soviet army spent ten years in Afghanistan. This war entered its third week with the Americans battering through Iraq's Republican Guard divisions to the gates of Baghdad. At this rate, it will be a surprise if the Americans have to fight for ten weeks, let alone ten years. Israel's occupation of the West Bank and Gaza has lasted for 36 years. If America has its way, its occupation of Iraq is more likely to last for fewer than 36 months. And there is no reason why America should not have its way: unlike Israel and the Palestinians, America and Iraq have no territorial quarrel. America's stated aim is to remove the regime and its mass-killing weapons, allow the Iraqis to replace their dictatorship with a representative government, and then depart.

By sticking to this plan and remembering to go home, the Americans should be able to reduce the

damage their victory does to wider Arab pride. They and the British are already going to unusual lengths to bring some delicacy, even political correctness, to the battlefield. There is no tactless raising of the Stars and Stripes or the Union Jack over captured Iraqi positions. The civilian casualties, which even the Iraqis put at under 1,000, have so far been negligible by the standards of war.

When the war is over, especially if its ending emboldens Iraqis to say out loud that they abhorred the previous regime, Iraq will make an improbable Afghanistan. The Arabs who flocked to fight in Afghanistan had a superpower (America) on their side and a base (Pakistan) to fight from. They also had an idea: they were fighting for Islam against communist atheists. None of this applies in Iraq. Iran and Syria, already on George Bush's watch list, have good reasons not to pick a fight with America. Iraq's other neighbours—Jordan, Turkey, Saudi Arabia and Kuwait—are already America's friends. Some of these governments will no doubt seek spheres of influence inside the new Iraq. This is a danger. But none will risk making itself the base for an anti-American guerrilla war. However much they disapprove of this war, most Arab governments will stay on side. And those that do not stay on side will stay in line.

Devoid of heroes, and short of ideas

The governments may stay in line. But what about the people? Here too the danger of an Arab explosion is greatly exaggerated. There has been much loose talk in recent weeks about the possibility of the Iraqi war reviving the spirit of pan-Arab nationalism. But this idea of uniting the Arabs in a single polity expired a long time ago. In an irony, it was Mr Hussein who administered its death blow, when in 1990 he invoked the broader Arab interest as a reason to invade Kuwait, and so forced many other frightened Arab states to take America's side against him. Today's Arab world possesses no leader with the charisma of a Nasser, who in the 1950s and 1960s seemed capable of reaching across borders to electrify the masses. Mr Hussein might—just—have been capable of achieving a similar status if he had prevailed against America in the Gulf war, or if by some miracle he were to prevail now. But if he is defeated and disappears, his influence will flicker out.

If secular nationalism has failed the Arabs, will they turn to violent Islamism instead? It is unlikely. Over the past 20 years, Arabs have watched the Islamic revolution in Iran, which once hoped to export revolution to the Arabs as well, fail in war against Iraq and then fail in economics too. In countries where radical Islam turned violent, such as Egypt and Algeria in the 1990s, it has succeeded mainly in scaring the middle classes and secular intellectuals, who might otherwise have pushed for political reform, into accepting ruthless state repression. A few pious and violent hearts, offended by the spectacle of infidel intrusion, will no doubt respond to the Iraqi war by taking up arms alongside al-Qaeda. But though some Arabs admired the attack on the twin towers, most know that religious war against the West is no answer to their difficulties. The chances of Iraq igniting such a war is slim.

All this is reassuring. But it is reassuring only up to a point. It means that the Arabs have no dangerous answer to their problems, but it does not mean that they have no dangerous problems. On the contrary: to the problems of authoritarian governments, rising populations and failing economies, a successful American war in Iraq is liable to add a new dose of bitter humiliation. The glee with which so many Arabs have woven a myth of David-beats-Goliath resistance around Iraq's early performance in this war points to the danger of dreadful let-down when the reality of the regime's reverses sinks in. Even a short war in which the coalition bends over backwards to show that it is fighting the Iraqi regime and not the Iraqi nation will leave a bruise on Arab sensibilities. In 1967, six days of war was time enough for Israel to humiliate a generation of Arabs. Lately, a new generation has fumed helplessly as Israel knocks the stuffing out of the Palestinian *intifada*. Now Arabs are having to fume helplessly while Israel's superpower patron knocks the stuffing out of the one Arab state that had set its heart on becoming a superpower itself. To judge by the rage in Cairo, Damascus and other capitals, it is more than many Arabs can bear.

Humiliation is a dangerous thing. What is worse is that there is not much the western powers can do to soothe the wounds. In Iraq, America and Britain believe correctly that they are acting in their own vital interest and that of the wider world by separating Mr Hussein from his mass-killing weapons. They can try harder to bring peace to Palestine—indeed, to create a Palestine—but this will be possible only if the Palestinians and other Arabs stop hoping that they can reverse what many still see as the humiliation of Israel's creation. They can try to create the conditions in which a post-Saddam Iraq can become an exemplary democracy. But what if Iraq cannot rise to the occasion? Ultimately, it is for the Arabs themselves to opt for the modernity and democracy that have eluded them. All this war can do is to make that possible. It cannot guarantee that it will happen.

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Affirmative action

End it, don't mend it

Apr 3rd 2003
From The Economist print edition

The time for affirmative action has passed

AP

Get article background

THE latest struggle in America's two decades of anguish over racial preferences is grinding towards a possible conclusion. The Supreme Court this week heard the most significant race-discrimination case for a generation (see article). Emotions are running high on both sides of the debate. Despite this, the court should not merely tinker with the concept of affirmative action, as it has done in the past. It should boldly rule out the use of race as a factor in university admissions, setting aside an outdated idea which is now doing America more harm than good.

In 1997, three white students with good marks were denied places at the University of Michigan, one at its law school. All three sued the university for discrimination, arguing that academically less-qualified black and Hispanic students were admitted instead. In deciding their cases, the Supreme Court's nine justices will rule whether universities, public or private, may continue to discriminate on the basis of race. Twenty-five years ago, the court forbade the use of explicit racial quotas but offered the idea that race could nevertheless be used as a “plus factor” in considering aspiring students.

That logical fudge left the door open to racial preferences which all too often work exactly like quotas. The University of Michigan's programme—which weighs skin colour even more heavily than standardised-test scores—is merely one of the more extreme examples. Others use less explicit, but equally discriminatory, formulas. Though all of America's top universities deny having a racial quota, this is what their policies amount to in all but name.

Affirmative action's original rationale was to redress past racial wrongs. This made sense. America's blacks were victimised first by slavery and then a century of legal, and frequently violent, discrimination. They could not be expected to shed immediately the shackles of the past, and to compete without help for places at university and the best jobs. But affirmative action was only really justified as a temporary measure. Nearly 40 years after America's landmark civil rights act, the time has come to live up to the ideal of race neutrality.

Instead, affirmative action has become a permanent feature of American life. Now its rationale, supported not only by America's top universities, but also most of its large companies and even its military, is the pursuit of “diversity”. But this is a poor argument for making racial discrimination a permanent evil.

The most recent census shows the old black-white divide breaking down in America. A larger fraction of Americans than ever say they belong to more than one race. Should the offspring of Tiger Woods, a multiracial golfer and millionaire, be eligible for racial preferences? Today there are more “Hispanics”, a racial category invented in America which also benefits from affirmative action, than blacks. In five or six decades, whites may be a minority. Should they too then become eligible for affirmative action?

Of course not. Defenders of racial preferences paint a bleak picture of a world without affirmative action. But there are many other ways of fostering diversity while treating each person as an individual rather than as a representative of a racial group. Universities should still be free to take students' backgrounds into account: whether, for example, they come from a poor home, or have surmounted personal obstacles. California's universities, where racial preferences were banned in the 1990s, have used such schemes to create diverse student bodies without using race.

Schools, the real battleground

It is a pity that elite universities have become the focal point for America's racial rancour. For this obscures the real place where discrimination occurs: through woefully inadequate education for huge numbers of poor minority students. Fixing this problem is less glamorous and more difficult than engineering the ethnic mix at elite colleges and law schools, but it would help far more people.

The time for affirmative action has passed. A majority of Americans say they oppose using skin colour to allocate university places and jobs. Across the world, in India, Malaysia, South Africa, and Brazil, racial preferences have caused needless strife. America's Supreme Court should send a message to the world that it takes seriously the words of its constitution, which affords “equal protection of the laws” to all its people. Racial preferences are an affront to this principle, the foundation stone of any decent society.

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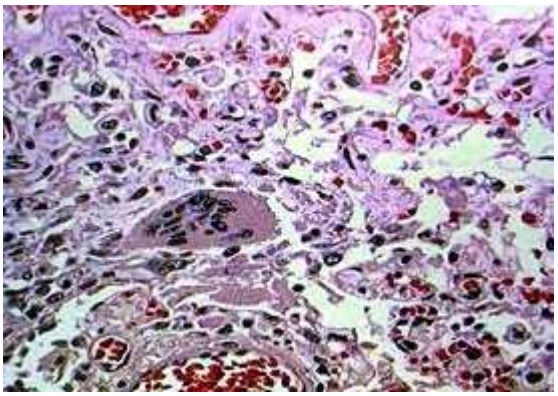
The SARS virus

Coughs and sneezes

Apr 3rd 2003
From The Economist print edition

Caution in the face of a new disease is justified

AP



EPIDEMICS, like wars, bring out strong emotions. Fear and anger are chief among them, as can be seen in Hong Kong, where a new viral disease, Severe Acute Respiratory Syndrome (SARS), is raging. The viruses that cause SARS are formidable foes. They are invisible attackers, spreading with alarming ease across continents, and of unknown strength.

Since the first case was officially reported in February, SARS has spread to 18 countries, leaving more than 2,200 people feverish and gasping for breath, and killing 78. The disease seems under control in Hanoi and Singapore, but it is still rampaging through Hong Kong and Guangdong province in China, where it is thought to have originated (see article). This week, the World Health Organisation (WHO) followed America's State Department in advising travellers to put off “non-essential” visits to both areas until further notice. Most people have not waited: Hong Kong is a ghost town. Offices are shut, conferences cancelled, schools closed and businesses right across the region are reeling.

The question is, are people overreacting? After all, only 4% of those laid low by SARS have died so far. Ebola fever, to take a contrasting example, can kill 90% of those infected. It is not, though, the deadliness of SARS that urges caution, but its novelty. SARS is not an age-old affliction like plague or cholera, with well-established modes of transmission and means of control. While public-health teams have determined quickly what causes SARS, how to diagnose it and how best to treat it, they are still unsure how it spreads and how long it will last.

As Britain's sorry story of mad-cow disease illustrates, in the face of such uncertainty, precautionary measures, however painful, probably cost less in terms of lives, dollars and blame than telling people to carry on with business as usual. Warnings not to travel to the region, and even measures of quarantine on those coming from it, accordingly seem justified for the time being. If China objects, one good response is that it was the failure by the Chinese authorities to inform the outside world that they had an unusual disease on their hands that robbed researchers of vital time to work out what was going on. The earliest cases of SARS emerged in Guangdong in November, but the WHO first heard about the disease in February—and even then through unofficial channels.

Political machinations, combined with a culture of secrecy, mean that China has a bad record in coming clean about disease, as its emerging AIDS epidemic also shows. Although the Chinese government has worked out a plan with the WHO to detect and monitor influenza epidemics, it has not implemented it. Only this week did it belatedly agree to let in WHO experts. Such recalcitrance is unacceptable. If China wants to be taken seriously as a modernising (if poor) country, it must deal more openly with disease

risks that could affect its partners through trade and travel.

China may be an extreme example, but it is not entirely alone in being slow to detect and respond to sudden outbreaks of disease. America is beefing up its surveillance network to deal with the threat of bioterrorism. But most places where new diseases are likely to emerge are poor, lacking not just money but also machines and trained manpower to detect and deal with them. Aid donors who are paying for the fight against AIDS, tuberculosis and malaria should also help to beef up poor countries' public-health systems for monitoring and controlling disease. Forewarned is forearmed.

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About sponsorship

Zimbabwe

Bringing down Mugabe

Apr 3rd 2003
From The Economist print edition

Zimbabweans have little option but to take to the streets

Get article background

IT IS always a bad idea to compare an adversary to Adolf Hitler. The comparison never rings true, and you end up sounding silly. But what do you do when the object of your disapproval compares himself to Hitler, as Robert Mugabe, Zimbabwe's president, did last week? In fact, he went further than that, describing himself as “Hitler tenfold”. Mr Mugabe's critics, who probably include most of the people of Zimbabwe, may feel that he has stolen their thunder.

To be clear about this, despite what he says, and despite the two men's similar racist rhetoric and moustaches, Mr Mugabe is no Führer. He may rig elections, goad his militia to torture dissidents and deny food aid to people suspected of supporting the opposition (see article), but he has not yet tried systematically to exterminate everyone he hates.

Mr Mugabe does not resemble the Nazi leader in the way he would like to think he does, either. He compared himself to Hitler because he sees himself as a nationalist strongman standing up to British imperialism. He argues that all Zimbabwe's problems stem from Britain's attempts to crush his regime. But the truth is that neither Britain nor any other western power has made more than token efforts to curb Mr Mugabe, because he poses no threat to their vital interests. If the people of Zimbabwe desire a change of regime (and it is obvious that they do), they can expect little outside help.

The main Zimbabwean opposition party, the Movement for Democratic Change (MDC), is at last waking up to this reality. Its leader, Morgan Tsvangirai, was so confident that he would win the presidential election last year that he appears to have drawn up no plan B. Indeed, he would have won that vote had Mr Mugabe not cheated on such a heroic scale. Since then, the MDC has floundered, one day promising protests to unseat the illegitimate government, the next day backing down for fear that Mr Mugabe will massacre protesters.

In recent weeks, however, Mr Tsvangirai has stirred himself. A general strike last month brought cities to a standstill, and rattled the regime enough to prompt it to arrest more people than usual. Mr Tsvangirai gave Mr Mugabe an ultimatum. If, by March 31st, he did not make certain concessions, such as stopping the harassment of MDC supporters and the politicisation of food aid, he would face “mass action”. Predictably, Mr Mugabe ignored the deadline. What next?

Every option appals

Mr Tsvangirai is pursuing a dangerous strategy. He may be more popular than Mr Mugabe, but the government has all the guns. If Mr Tsvangirai summons up big, angry crowds, Mr Mugabe's men may simply shoot them. But if he does nothing, the regime will stay in place, the country will continue to grow poorer, and legions of Zimbabweans will continue to weaken from hunger and succumb to the diseases of poverty.

Outsiders could do more to help. The European Union, America and other western countries have slapped limp sanctions on leading members of the regime. They could increase the pressure by, for example, pursuing the ruling party's business associates, especially those who have helped the Zimbabwean army to loot Congo, where it was sent in 1998 to prop up another despotic regime. But a wider trade embargo is out of the question, as it would hurt ordinary Zimbabweans, not their rulers.

South Africa's president, Thabo Mbeki, has sought to push Zimbabwe's opposition and ruling party into power-sharing talks, an approach he favours because it worked in South Africa a decade ago, and which he has urged, with some recent success, on warring parties in Congo. But it has failed in Zimbabwe because Mr Mugabe has no intention of sharing power. It would be helpful if his party could persuade him to retire. But it would be foolish to assume that it will even try. Foreigners should not, from a safe distance, be urging Zimbabweans to risk their lives. But if they protest loudly and peacefully, we should applaud.

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About sponsorship

Illicit drugs

Breaking convention

Apr 3rd 2003
From The Economist print edition

Time to think again about the rules of engagement in the war on drugs

Get article background

WHATEVER illicit drugs do to the behaviour of those who consume them, their effect on policymakers is to destroy common sense. Next week, a big meeting in Vienna will review the progress countries have made towards eradicating or significantly reducing the use of such drugs by 2008. This goal has receded since it was set at a special session of the United Nations five years ago. Vienna will gloss over failure with much blether about tough new policies. But the most sensible policy—a review of the three UN conventions that set the ground rules for fighting the war on drugs—will be ignored.

Curbing the drugs trade needs global rules. International agreement restricts some other trades that governments want to discourage—in endangered species or hazardous waste, for instance—although the UN does not yet tackle trade in guns or tobacco, two of the world's biggest killers. But the drugs conventions cover not just trade but production, manufacture and even possession. They require signatories to make possession of drugs, including cannabis, a criminal offence (see article).

Many signatories would choose such policies of their own volition. But a number of countries in Europe and the Commonwealth, as well as some American states, would like the freedom to experiment with other approaches. Some think it ludicrous to make criminals of users of cannabis, a drug that (unlike tobacco and alcohol) rarely leads to fatalities. Others worry that the sharing of syringes is one of the main ways that AIDS spreads, and want to concentrate on reducing the harm drugs do, even if that means tolerating their use.

Such countries can generally find legal loopholes in the treaties. But the loopholes stretch only so far. For example, several governments do not prosecute those caught possessing cannabis for personal use. This hands a bonanza to criminals who control a trade that is still illegal. Only if cannabis—and other drugs—can be legally produced and traded can a government regulate quality and outlets, and only then might reputable companies emerge, willing to offer a safe product.

Living with drugs

What is the alternative? As David Bewley-Taylor, a British academic at the University of Wales, Swansea, argues in the current issue of the *International Journal of Drug Policy*, scrapping any of the treaties is politically out of the question: too many countries would veto such a move. If any country backed out, it

would attract the fury of America, which has found it convenient to repudiate other UN treaties from time to time, but takes a hard line on drugs. Even so, a group of like-minded countries might give each other courage; and the 1988 treaty appears to allow countries to do without criminal laws against drugs if their courts find such laws unconstitutional.

Such a dissidents' club might be accused of encouraging a trade that finances global terrorism. But a legal and tightly regulated trade would actually snatch profits from terrorists and criminals. Nobody accuses the world's cigarette smokers of financing bombers. Yet not only is tobacco a killer; cigarette smoking among the young is correlated with consumption of other drugs. The World Health Organisation (WHO) has been negotiating its first treaty on tobacco, due for approval by its members this year. But the treaty will not prohibit the cultivation of, trade in, or possession of tobacco. Perhaps a proposal to add tobacco to the UN drugs conventions would help to bring common sense to the war on drugs.

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Letters

Apr 3rd 2003
From The Economist print edition

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Iraq and the Shias

SIR – You mention "profound sectarian divisions" in Iraq and raise the question of whether the people of that country have a common identity ("What kind of victory?", March 22nd). In fact, the potential for sectarian secessionism, particularly by the Shias, is often exaggerated. All the main Shia opposition groups support the continuance of a unified Iraqi state.

Despite the fact that Saddam Hussein's abuses were often directed at specific ethnic or religious groups, the expected backlash is more likely to be directed at members of the regime, and those associated with it. This was certainly the case during the Shia uprising in 1991, when revenge attacks were not targeted on sectarian grounds but encompassed Sunni and Shia collaborators alike.

The main risk of sectarian division comes from foreign states sponsoring particular armed groups or the crude power-sharing proposals currently being considered by America, which threaten to entrench ethnic or religious differences. The most important post-conflict step towards the further development of a common national identity would be the instigation of a constitution-drafting process that involved all Iraq's different communities. For the Kurds, crucially, that would hold out the promise not just of retaining real autonomy but also gaining fair participation in national government.

Mark Lattimer
Director
Minority Rights Group International
London

SIR – When will you guys admit you are wrong? Your coverage of Iraq is disappointing, shallow and worst of all, inaccurate. You predicted Germany would look foolish when France capitulated. You were wrong. You predicted that America would be vindicated after American intelligence guided inspectors to sites of weapons of mass destruction. You predicted the Shias would rise up to welcome the invaders as "liberators". Wrong yet again. You say the military campaign is doing well. Yet this war is a complete fiasco.

The reputation of America is being destroyed as al-Jazeera beams the carnage of Baghdad around the world. Hatred of America and the risk of terrorism grows daily. Iran and North Korea rush to build the nuclear weapons that will give them security. Friendly regimes around the Middle East brace themselves against public outrage. Coalition soldiers are welcomed with bullets instead of flowers. And to what end? A long and bloody occupation under Jay Garner, an American-appointed dictator whose strong support of Israel will surely render him ineffective as a leader to rebuild this nation?

Simon Stuart
Morristown, New Jersey

SIR – I watch the many war protesters on television and wonder whether they are really against a war or, more likely, are anti-American. Where were they when NATO, under American leadership, bombed Serbia into submission? What makes Saddam so different from Slobodan Milosevic? I see consistency from America; I see people closing their eyes to French, German and Russian business interests in Iraq.

Erik Aasterud
São Paulo

Friends in high places

SIR – Your uncritical cheerleading for the Bush administration goes too far in suggesting that there is no relationship between Dick Cheney's role as America's vice-president and contracts won by Halliburton ("Cheney's cronies?", March 22nd). What better lobbyist for government business could a corporation wish for than the vice-president himself?

In the same issue you point out that Jean-Luc Lagardère and Gianni Agnelli used "a valuable talent anywhere...dynastic ties and political connections to control and develop their empires" (Face value, March 22nd). Is it just perfidious Europeans who stoop to such influence?

Keith Ashfield
Arroyo Hondo, New Mexico

Tax and defend

SIR – You overlook the primary determinant of an American soldier's domicile: state income taxes ("Don't mess with Texas", March 22nd). Texas, Florida, Washington and Alaska are among the few states that do not impose an individual income tax. Not surprisingly, many soldiers switch their "home states" upon enlistment to take advantage of this quirk in the law. Those serving in the military who (unwisely) claim domicile in New York should seek tax advice from their fellow soldiers.

Todd Hansen
Brussels

Pouring cold water

SIR – Many governments in developing countries are failing to bring water to their populations, particularly the poorest ("Bogged down", March 22nd). However, the blanket promotion of private-sector participation as the solution, particularly by donors such as the World Bank, is misguided. It does not tackle the underlying causes of the problem such as lack of community involvement, weak regulation, and a shortage of government knowledge, interest and expertise. Recent research by Tearfund and WaterAid shows that private-sector involvement is not working in practice, particularly for the poorest people.

The capacity of the public sector must be addressed, not ignored in favour of the private sector. Any reform of a public utility needs a well resourced, efficient and effective government to facilitate it successfully. Without this there will be, for example, little or no regulation of private activities (something that private companies actually want). Tearfund believes that a fundamental rethink is needed—one that will mean a move away from the obsession with the private sector and towards people-based water services that are rooted in communities and local authorities.

Joanne Green
Tearfund
Teddington, Middlesex

Solitary pleasures

SIR – I am shocked by your review of "Solitary Sex: A Cultural History of Masturbation" but I should not have been surprised ("One and only", March 15th). The *San Francisco Chronicle*, a family newspaper, recently published an essay describing at great length the virtues of the solitary vice. I immediately wrote to the author, a part-owner of Good Vibrations, a sex shop, and asked why she had not written the article 65 years earlier, when I had been taught a totally different lesson in my school "hygiene" class. The instructor informed us then that he could tell, just from looking at our eyes, if we had been playing with ourselves—and added that, as the school's wrestling coach, he would never permit such perverts to join his team.

That warning devastated me because my greatest goal in life then was to participate in this manly sport. And judging from your other book review on the importance of luck in American life, who knows how far I could have gone if I had not been blackballed from the team ("How they made their luck", March 15th)? After all, the present speaker of the House of Representatives is a former college-wrestling star.

William Burke
San Francisco

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War in Iraq

Misgivings fade at the city gates

Apr 3rd 2003
From The Economist print edition

AP

The campaign approaches its climax as coalition troops advance on Baghdad

Get article background

BY APRIL 3rd, the American war machine rumbling up the roads to Baghdad was within spitting distance of its destination. The resistance offered by the Republican Guard divisions arrayed around the capital had, so far, been less impressive than their sonorous names. The battle for Baghdad may be quick or protracted, but the resumed coalition advance marks at least the end of the beginning, and perhaps even the beginning of the end. All this makes the sideshow war inside the Washington beltway about America's war plan seem pre-emptive, to say the least.

To those immersed in the round-the-clock television coverage of it, the fortnight-old war in Iraq sometimes seems to have lasted much longer. That warped perception of time has been partly responsible for the doom-mongering that hummed beneath the noise of battle during the campaign's second week. The dramatic northward thrust from Kuwait by coalition forces was followed by what seemed—but only seemed—a relative lull.

Cue the doomsayers, arguing that Donald Rumsfeld, America's defence secretary, miscalculated what it would take to defeat Saddam Hussein. After a suicide bombing killed four Americans at Najaf on March 29th and then, nearby and soon afterwards, at least seven Iraqi civilians were shot dead at a checkpoint by jittery American soldiers, it seemed that American heavy-handedness risked alienating both ordinary Iraqis and global opinion.

What evidence was there that the plan was unravelling? A few serving officers remarked on the unexpected determination of some Iraqi fighters, and some retired ones roused themselves to denounce the plan on television. The charge is that Mr Rumsfeld and his like-minded civilian sidekicks coerced General Tommy Franks, who is running the war, into embarking on it with fewer troops than he needs. Mr Rumsfeld allegedly wants to vindicate his belief that air power and light ground forces can, with America's stellar technology, transform the way the country fights its wars. Thus he repudiated the “Powell doctrine” of overwhelming force, rejected requests for extra troops, and scotched the idea of a delay after Turkey hobbled the plan for a proper northern front.

For part of the last week, these complaints were given some credibility by a widespread perception that

the coalition advance had stalled. One of the other distortions caused by the blanket television coverage is that it turns hearsay (an armoured column heading out of Baghdad; an uprising in Basra) into news, and inflates minor setbacks into major reversals. Strategic overview can get lost amid all the tactical excitements—or, as was the case for a few days last week, the lack of them.

Only a handful of people truly know the war plan's history or contents, and two of them—Mr Rumsfeld and General Richard Myers, the chairman of the Joint Chiefs of Staff—this week defended it vigorously. Mr Rumsfeld (certainly a hands-on boss) stressed that General Franks was the plan's main architect. He admits that Turkey's snub was a disappointment, but argues that, having forfeited strategic surprise through the military and diplomatic build-up, the coalition salvaged some tactical surprise by attacking when it did.

But the gossipy question of the strategy's genesis is infinitely less important than whether it is working. Despite all the carping, the short answer remains yes.

Meanwhile, in Iraq

On television, the war seemed to have paused; and, says Andrew Krepinevich of the Centre for Strategic and Budgetary Assessments, a Washington think-tank, some American ground forces may have paused: “but there was no pause for the Republican Guard.” The divisions of Mr Hussein's elite force guarding the southern approaches to Baghdad have, with growing intensity, been pounded by coalition aircraft and artillery. Their tanks may be less conspicuous than was the Iraqi armour during the desert confrontations of 1991, but many are still more accessible than if Mr Hussein had withdrawn them within Baghdad itself. American commanders estimate that some Iraqi units have lost half their fighting capacity; the Baghdad Division, stationed to the city's south-east, is said to have been destroyed.

After earlier skirmishes, on April 1st American land forces began seriously to engage what remained of the Guard across and beyond a broad arc between Karbala and Kut. America's Third Infantry Division pushed through the “Karbala Gap” between the Euphrates and Lake Razzazah, and on April 3rd was closing in on Baghdad's main airport. The marines had crossed the Tigris; dams that could have been destroyed to impede the advance were seized. Further south, the 101st Airborne Division was subduing Najaf, where Saddamite diehards had holed up in a Shia shrine. Despite reports of some troops subsisting on one meal a day, the supply lines now seem secure.

With no heavy coalition forces advancing from Turkey, some Iraqi reinforcements from the north have made their way south. Nevertheless, there have been coalition gains in the north too. An Islamist terrorist group was routed by American and Kurdish forces. Supported by coalition air power, Kurdish troops are also closing in on the towns of Kirkuk and Mosul. In the south, British troops have made incursions into Basra and other nearby towns, shelling Iraqi forces on the city's fringes and enabling some civilians to flee. Some Iraqi civilians are warming to their conquerors, and a few are even assisting them: Iraqi tribal forces have reportedly fought alongside the coalition.

And although non-events are not generally considered newsworthy, it ought also to be remembered that several calamities that didn't materialise in the war's first week—large-scale terrorism, a strike on Israel, a chemical attack, strife between Kurds and Turks—failed to do so in its second week as well. (Mr Hussein's weapons of mass destruction have still not been found, either.) Coalition fatalities remain light. A high proportion have been caused by “friendly fire”, an issue that Britain and America ought to have addressed more urgently after the 1991 war; but the deaths thus inflicted would be less conspicuous if more coalition troops had been killed by Iraqis. The rescue of one young female soldier boosted American morale.

Still, if the Iraqi battlefield looks nothing like the catastrophe implied by some of Mr Rumsfeld's critics, neither is it quite the “catastrophic success” predicted by his cheerleaders. Neither the regime nor the Republican Guard has folded altogether. Despite what Mr Rumsfeld says about longstanding plans for reinforcements to arrive after the war began—around 2,000 troops are flowing into Iraq every day—some deployments do seem to have been accelerated. And there have been some tragic accidents and miscalculations: as well as the shooting in Najaf, an attack on the town of Hilla killed dozens of innocents, and cluster bombs have reportedly been dropped in civilian areas (reprehensible, if true). In Baghdad, where allied bombers and missiles seem to have been targeting communications facilities, a maternity hospital was reported hit on April 2nd. Some American troops might profit by the example of tactics used by the British in their interactions with the locals in southern Iraq.

These tragedies have provided Mr Hussein's regime with ammunition for its propaganda campaign, one of the few weapons left in its armoury. Another strategy it would like to develop is suicide bombing: with wild, bin Ladenesque rhetoric, Mr Hussein exhorted potential martyrs in a message delivered (mysteriously) by his information minister. The coalition has countered with credible tales of torture, summary execution and wholesale violations of the rules of war, and by casting aspersions on the health and well-being of Iraq's dictator.

Yet even according to the official Iraqi count, civilian fatalities are not yet overwhelming. Maintaining the same level of sensitivity in the urban battle that now looks imminent will be a challenge. Should Mr Hussein deploy chemical weapons—always most likely once he is ineluctably cornered—the complexion of the war will change. With or without them, the street fighting is likely to be gruesome.

So, as Mr Rumsfeld himself says, “it's a little early to write history.” In two other recent conflicts—the Kosovo war, for much of which it was widely argued that air power alone could not beat the Serbs, and in Afghanistan, generally touted as a graveyard of empires—conventional wisdom ended up looking foolish. Of course, the war in Iraq may yet turn out to be the strategic failure that Kosovo was not, or the quagmire that Afghanistan never became. But it seems more likely that the doubters will again be proved wrong.

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Life in Baghdad

When confidence meets cataclysm

Apr 3rd 2003 | BAGHDAD
From The Economist print edition

On the very eve, Baghdadis were still optimistic

AP

The terrible swift swords are not theirs

Get article background

TWO weeks into the bombing of Baghdad, more and more people were itching to get back to normal. Shops, restaurants and offices were cautiously re-opening. Some people were bored at home; some needed to get back to earning a living. Even traffic jams returned.

One spice merchant in Baghdad's Ash-Shurja market, who had just opened up again and was bringing back stock which he had taken home for safekeeping, said he expected his friends to follow his example. And this despite the fact that explosions, caused either by American or British missiles or by misfired Iraqi anti-aircraft rockets, have killed at least 79 people in two Baghdad markets since the war began.

For the moment, those shops that are open have plenty to sell; the war was so long in coming that traders stocked up in advance. Fresh fruit and vegetables are still available, though prices are climbing because of uncertainty about the safety of the roads in and out of the city. Haulage firms are still offering to truck in imports, at a price, along the road from Damascus. Iraqi customs officials are still manning the border, but between them and Baghdad lie two American military checkpoints.

How long supplies in and to the city will last depends, of course, on whether the Americans and British really will encircle it. The feeling in Baghdad, despite the news of a new push on April 2nd that brought troops ever closer to the city, is that that prospect is receding. Early claims that various towns had fallen, that regiments had surrendered or that an uprising in Basra had started—all of which turned out to be untrue—have damaged British and American credibility. Iraqis now put more faith in Iraqi military communiqués than they do in reports from the other side of the lines.

Still, most Iraqis, after decades of repression and censorship, are pretty canny about gathering and interpreting information. Many listen to the Arabic Service of the BBC, Iranian radio and Radio Monte Carlo, among others. By fitting a special antenna they can watch Iranian television's Arabic-language channel, which shows foreign television footage of the war. These antennae are selling fast.

Meanwhile, Iraqi television is showing morale-boosting videos of a choir that travels round Baghdad, recording songs at various places every day; clips from al-Jazeera and from Syrian TV; some discussion of the situation; and film of captured British and American equipment and dead soldiers. Iraqi television

has interviews with foreign and local fighters who chant their undying love for Saddam and dance with guns waved aloft, sometimes on top of or around a piece of captured equipment. Their womenfolk are shown stirring huge cauldrons of food for the fighters, waving their ladles in the air and shouting their defiance.

By comparing notes with friends and neighbours, and of course gleaning information from people who have been travelling or seen action, Iraqis, each of them with a few pieces of the puzzle, build a picture of what is happening. A few months ago, satellite television—offering a restricted menu mostly of entertainment channels—was allowed in Iraq, but since the war began it has gone off the air.

For late-night viewing, Iraqi television prefers films with a topical message. These have included one about Saladin, the (Kurdish) warrior who drove the crusaders out of Jerusalem, a film about the Iran-Iraq war and one about the Egyptian crossing of the Suez Canal in 1973. Unsurprisingly, that one stopped short of showing the Egyptian defeat that soon followed.

The conclusion that Baghdadis are beginning to draw from all this is that their government has shrewdly wrong-footed the coalition forces. There is a growing pride in the fact that not one town of size has been captured, and that their defence has been achieved by relatively small groups of determined militiamen rather than regular soldiers. Now, more people who might have simply shrugged off, or even welcomed, the fall of Saddam are beginning to think about fighting for Iraq, if not for its president.

However they are caused, the increasing civilian casualties are also stirring anger. At 5.30 in the evening on March 28th an explosion killed 62 people, including many women and children, in the packed marketplace of al-Nasr in the al-Shula quarter of north-west Baghdad. The crater was extremely small, but eyewitnesses said they had seen both a plane and a missile. Whether the missile was fired by the plane, which locals believe, or was a misfired anti-aircraft rocket, is hard to say. What is clear is that this tragedy, in a Shia area, has damped hopes that the Shias of Baghdad would stage an uprising in America's favour as the troops advanced.

As the conflict drags on, and despite the increasing normality on the streets, most families find themselves stuck at home all day. Schools remain shut; many men are ordering their children, and often their wives too, to stay at home. In areas where there are many bombing targets, especially on the outskirts of the city, sleep is hard and children are frightened. All this is beginning to take its toll. The Americans say they want to bring democracy to Iraq, people mutter. But is this democracy?

Hospitals, thus far, have been able to cope. They have been making preparations for months, if not years, assembling stocks of medicines and recruiting many well-trained doctors who have field experience from the Iran-Iraq war or the Gulf war. As a result, many foreign doctors who have come to help have been left trailing around hotels in central Baghdad with nothing to do.

In absolute numbers the figures for casualties are, for the moment, manageable. The Iraqi authorities claim that, since the war began, at least 500 civilians have been killed and 4,000 wounded across the whole country. Roland Huguenin-Benjamin, the spokesman for the International Committee of the Red Cross in Baghdad, says his teams are reporting that, on average, 100 wounded civilians arrive in the city's hospitals each day. Of these, about ten to 15 are seriously injured. The Red Cross has 7,000 surgical operations kits available, but so far the authorities have not asked for them.

Apart from civilian casualties and uncertainty about the roads outside the city, Baghdadis are most infuriated by the targeting of the city's telephone system. So far, electricity and water supplies have been left untouched; but attacks on telephone exchanges have left large parts of the city with no phone lines at all. A single raid on the Bab al-Mua'dam exchange, on the night of March 30th, took out 25,000 lines. Most lines out of Baghdad have been cut, as have all international ones. This means that Iraqis cannot keep in touch with anxious family members in other parts of the country or abroad. The British and Americans point out that telecoms also have military uses. But, even if they have, most Iraqis neither know nor care.

The raid on the Bab al-Mua'dam exchange also killed the small son of one of the workers there, who lived next door. Relatively few people are going to shelters or basements at night. Some who refuse to go are mindful of the American missile that hit the al-Amariyah shelter in February 1991. It killed 408 people, almost all of them women and children.

Besides, it seems to Baghdadis that the British and Americans are running short of targets to bomb in central Baghdad that will not risk large civilian casualties. Following a pattern set during NATO's bombing

of Yugoslavia in 1999, coalition aircraft are now coming back to hit empty buildings they have already bombed, including Mr Hussein's palaces and ministries. At about midnight on April 1st they came back to finish off the air-force headquarters. Though Mr Hussein has no air force that is flying, the building was totally flattened. Just in front of it, however, the statue of Saddam was left unscathed.

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Hearts and minds in southern Iraq

Softly, softly

Apr 3rd 2003 | NEAR BASRA
From The Economist print edition

We do it better, say the Brits

Get article background

THE only two “enemy” vehicles damaged in the fighting for the southern port city of Umm Qasr still lie on a dual carriageway, burnt-out and bullet-ridden. One is a lorry, its cab door pocked and melted by high-explosive missiles fired by men from Fox Company of the 15th Marine Expeditionary Unit.

Unfortunately, the vehicles contained no “enemy”, but a party of civilians desperate to flee from artillery and air attacks on the city. Two were killed instantly; four were severely injured. Accidents are common in war, of course. But standing amid the wreckage, next to vast puddles of spent American ammunition, it is hard to conclude that the marines were anything but trigger-happy.

At the Umm Qasr prisoner-of-war camp, the British officer in charge makes a similar observation. He has more than a thousand inmates to deal with, but only a few were ever involved with the Iraqi army or Saddam Hussein's regime. The almost daily rioting in the camp is caused not just by the awful conditions—flies, dust and heat—but by the resentment of people arrested willy-nilly by the Americans. Another officer gives examples. A goatherd has been arrested, so his goats roam untended; a man has been brought in, bruised and handcuffed, for asking an American patrol for help for his wounded daughter.

The campaign for the hearts and minds of Iraqis is more tortuous even than the war itself. In so-called Free Iraq, a piece of territory reaching in some places more than 320km from the Kuwaiti border, the attitude of the civilian population to coalition forces is, at best, ambivalent. Their experience of the American military juggernaut in the first few days of the war was brutal, and many among the British forces now grumble that they have been left to patch up the damage left behind.

The difference in tactics can be striking. When Fox Company thought it spotted “enemy” in a group of buildings, it fired missiles and mortars at the “position” for four hours. The next day, when a British patrol was fired at from a house in Umm Qasr, the six soldiers got out of their vehicles, approached the building on foot and arrested two gunmen. The incident was over in ten minutes, and no civilian property was damaged.

“For the Americans, there just does not seem to be anything between peace and all-out combat,'' says a British officer. “Their military doctrine remains one based on the use of overwhelming firepower in every circumstance.” British soldiers, though, can draw on 30 years patrolling in Northern Ireland and several years spent on peace-support operations in the Balkans. They know that a wide spectrum of grey lies between the white of peace and the black of war.

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Iraq's neighbours

Unacceptable behaviour

Apr 3rd 2003 | TEHRAN
From The Economist print edition

America has other worries in the region. First, Iran

Get article background

EPA

Uncomfortably close to Syria, too

A LITTLE over a week into the war, the Shia theocracy of neighbouring Iran called tens of thousands of people on to the streets to deplore it. That day, March 28th, happened to be the one on which Donald Rumsfeld, America's defence secretary, warned Iran's proxy in northern Iraq, an Iraqi Shia militia called the Army of Badr, not to take any part in the battle or else it would be considered hostile. Are Iran and America on a collision course?

It suits hard-line Iranians, puffing on the dying embers of popular anti-Americanism, to present things that way. Sharing a neighbourhood with countries whose citizens despise George Bush without prompting, senior conservatives had been embarrassed by Iranians' apparent indifference to the war. As non-Arabs who suffered horrendously while fighting Saddam Hussein in the 1980s, some Iranians even welcome Iraq's misfortune. Before March 28th, Iran's biggest anti-war demonstration had attracted only 700 people.

In fact, despite the daily praise on state television for the Iraqi resistance, the Iranian government has co-operated with the United States far more than might be supposed. Iran has taken a phlegmatic view of the stray missiles that have landed on its territory. It is relaxed, too, about the flagrant violations, by American and British military craft, of its coastal waters and airspace. Mr Rumsfeld had even offered mild praise earlier in the week, saying that Iran had “not done things that are making our life more difficult”.

Iran has also decided to seal as much as it can of its 1,300km-long border with Iraq. This is partly to deter refugees, though it is prepared to accept some. More crucially, the closing of the border seems to confirm that Iran does not intend to engineer a repeat of 1991, when the Army of Badr, accompanied by members of Iran's Revolutionary Guard, crossed the border to piggyback on a big Shia uprising. That rebellion was crushed by Mr Hussein after the elder George Bush, alarmed by Iranian adventurism, withdrew his support for it.

It may be that Mr Rumsfeld has information about the intentions of the roughly 5,000-strong Army of Badr force that is currently sitting idle in Kurdish-run northern Iraq. Before the war, this force seemed intent on trying to seize control of some towns—bargaining chips, so they intended, for the political carve-up after Mr Hussein's expected fall.

Having built up the Army of Badr's political wing, the Supreme Council for Islamic Revolution in Iraq (SCIRI), America has decided that Ayatollah Baqer al-Hakim, the SCIRI'S Iranophile leader, cannot be trusted. Furious at being sidelined, Mr al-Hakim has teamed up with his former rival for the affections of Iraq's Islamist Shias, the Islamic Call Party (Hezb al-Dawaa al-Islamiya), to condemn the invasion. Yet, perhaps because they fear being ignored, neither has called on Iraqis to rise.

According to Abu Bilal Adip, the Islamic Call representative in Iran, recent *fatwas* in which senior Shia clerics in Iraq called for a popular defence of the regime were exacted under duress. But he claims to know of an instance in the past few days of American forces holding back from helping an incipient uprising by the inhabitants of a town in the Euphrates basin. Such tales reinforce the suspicion among

Iraqi Shias that the Americans and British may not be forces of liberation, after all.

Iran's foreign minister says that Iran will not recognise a government installed by the Americans. If it is to retain any influence over its western neighbour—a feat it managed in Afghanistan, to the east—its Shia friends will have to attain positions of power. If Mr Hussein goes, but at a price that dissuades America from embarking on regime changes elsewhere, the clerics may even cheer.

At the weekend, Colin Powell, America's secretary of state, demanded that Iran end its support for terrorism and that it stop seeking weapons of mass destruction and the means to deliver them. America is watching to see whether Iran gives sanctuary to fleeing members of a radical Islamic group which its forces and the Kurds have prised from their northern Iraqi redoubt (see article). Short-term co-operation, the Americans seem to be saying, will not exempt Iran from having to adopt, in Mr Powell's lofty phrase, “acceptable patterns of behaviour”.

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Syria's role

Fierce words, tied hands

Apr 3rd 2003 | DAMASCUS
From The Economist print edition

Syria hates the war, but is too weak to play the spoiler

Get article background

THE veteran foreign minister, Farouk Sharaa, does not mince words. Syria, he says, has a national interest in expelling America and Britain from Iraq. The question he does not answer is: how far will Syria go to pursue that interest?

To date, it would seem, not very far. Syria's government has condemned the war more stridently than others in the region, and has sponsored the biggest street demonstrations. It has allowed Arab volunteers to trickle over its border to bolster Iraq's army. And, according to Donald Rumsfeld, America's secretary of defence, Syria has also connived in supplying military gadgetry, including night-vision goggles, to Baghdad.

Small wonder that Syria should collude. The two countries have much in common. The people of the Euphrates Valley in eastern Syria are near cousins to the Iraqis downstream. Both governments share the same militaristic, secular and xenophobic brand of Arab nationalism, although their rival branches of the Baath Party have often feuded. The relations of both with America have mostly been tense, but sometimes surprisingly close.

In recent years, Syria has been able to mute American criticism—of the succour it gives to extremist guerrilla groups and of its role in Lebanon, among other things—by providing useful intelligence against al-Qaeda. It has also balanced pro-Iraqi rhetoric with quieter support for Iraq's foes, both in backing Resolution 1441 in the United Nations Security Council and in giving sanctuary to the Iraqi opposition. But Syrian room for manoeuvre, already small, is likely to shrink even further. If and when America completes its occupation of Iraq, Syria will find itself completely surrounded by American allies, and physically separated from its closest strategic partner, Iran.

Syria is already weak. Since the collapse of its Soviet ally, its army has fallen even further behind Israel's in technology. The Lebanese joke that it cannot withdraw its 20,000 “peacekeeping” troops in their country because the vintage Soviet trucks cannot make it up the hill. Its economy, too, is stalled. Syria is the only Arab country that is self-sufficient in food, but the main construction activity in the past two decades has been the extension of slums around Damascus. Faltering stabs at free-market reform have failed to mollify investors wary of cronyism and corruption. Warming ties with Baghdad in the past few years have put the country on a vital drip feed, as oil smuggled out of Iraq has been exchanged for Syrian consumer goods. By last year, this semi-illicit trade was said to account for nearly 20% of GDP. But it is bound to stop now.

The Syrians deny that they are shipping arms to Iraq. They also deny Israeli allegations that Iraq has sent some of its outlawed weaponry for safekeeping in Syria. There are rumours in Damascus that senior officers have profited from an arms trade, but businessmen say it is quite possible, given the murkiness of the Syrian power structure, that the top leadership was unaware of serious hanky-panky.

Mr Rumsfeld has described this trade as “a hostile act”. Colin Powell, the secretary of state, has added that Syria's government would have to bear the consequences of supporting “terrorist groups and the dying regime of Saddam Hussein”. America, said senior officials and the state-controlled press, was just trying to distract attention.

Syria's young president, Bashar Assad, is riding a wave of popularity as anger over Iraq stifles yearning for change at home. But his options remain limited. American forces will soon seal off Baghdad from the

Syrian border. The long-promised road map for Israeli-Palestinian peace, which Syria condemns as inadequate, is likely to be endorsed by the rest of the war-weary region. Mr Assad admires the Hizbullah militia in Lebanon and compares the Palestinians' suicide bombers to those who resisted the Nazis. Yet Syria is simply not strong enough, any more, to play the spoiler the way his father, Hafez, did in the past.

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The northern front

Partners against the axis

Apr 3rd 2003 | IRBIL, IRAQI KURDISTAN
From The Economist print edition

Some useful joint house-cleaning against extremists

Get article background

"IT IS here and yet you don't see it!" Thus Hoshyar Zebari, the urbane foreign-relations chief of the Kurdistan Democratic Party, describing the coalition's elusive "northern front" against Saddam Hussein. Pressed further, Mr Zebari stressed that the front was indeed active. But not, he cautioned, in a way that one might expect.

Despite the fanfare surrounding last week's arrival of 1,000 American paratroopers at a muddy airstrip 30 miles north of Irbil, and the constant flow of men and materiel to the region, Kurdish officials admit that the northern front will be a considerably downsized affair. There will be fewer American tanks, fewer American troops and fewer conventional military operations along the jagged 500km demarcation line that separates the Kurds from the Iraqi army. Instead, Mr Zebari speaks of special missions behind enemy lines in which American special forces and Kurdish *peshmergas* will work together.

Fortuitously, co-operation of a similar sort exists already. Last weekend, the forces of the Patriotic Union of Kurdistan (PUK), helped by American special forces and a barrage of missiles from the air, launched an apparently successful root-out-and-destroy operation against Ansar al-Islam, an extreme Islamist network that has been making life a misery for both PUK supporters and villagers and townsfolk in and around the town of Halabja, near the Iranian border.

American and Kurdish commanders who led the assault claimed it had turned up a list of names of suspected militants living in the United States and, perhaps, the strongest evidence yet linking the group to al-Qaeda. Documents found in the rubble of the town of Biyara, Ansar's nerve centre—computer discs and foreign passports, with Iraqi visas, belonging to Arab fighters from around the Middle East—could yet give substance to the Bush administration's claims that the group is a nexus of evil, possibly even linking Saddam Hussein to al-Qaeda. The group may also have been getting help from inside Iran, whence some of its fighters fled after the PUK's onslaught.

The operation may have had more to do with the war against terror than the war on Iraq. But for the Kurds—basking in rare American praise for their help—it could be a sign of things to come.

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Arab volunteers

A bus ride to martyrdom

Apr 3rd 2003 | CAIRO
From The Economist print edition

They'll die for Iraq, but not for Saddam

Get article background

THE Iraqis say 6,000 of them have poured in from across the Arab world. More like a few hundred, say reporters who have tracked volunteers heading to join Iraq's beleaguered army. Whatever the numbers, the recruits form part of an emerging mythologisation of Iraqi resistance. Celebrated already in Arab poetry and song, the war is beginning to take on epic tones that fuse the bravery of ancient Muslim warriors with more recent struggles for Arab independence.

The first of the volunteer “martyrs”, Thaer Osman, a 28-year-old Palestinian, received a hero's burial in a Beirut refugee camp this week. In the pantheon of fame he joins Ali Mungash, the grizzled Iraqi peasant who, Baghdad claims, shot down an Apache gunship with his hunting rifle. In Saudi Arabia, rhyming text messages praise Mr Mungash's feat. Jordanians stick his picture in their car windows.

Ghastly images of Iraqi civilian casualties have mobilised the volunteers. Computer hackers in the Gulf have beamed them to America, where they are popping up on commercial websites to shock unsuspecting web-surfers with the kind of gore that America's own networks shy from showing. Al-Manar, the slick satellite station run by the Lebanese guerrilla group Hizbullah, has taken to intercutting carnage in Iraq with Nazi atrocities.

Such imagery, mixing Iraqi stoicism and suffering with deeper collective memories, has provoked a wave of sympathy and outrage among Arabs and Muslims. And it has prompted a few to offer the ultimate sacrifice in what they see as the defence of Muslim soil against an infidel invader. “When we see women and children being slaughtered in front of us, would we be men if we didn't go?” demands a young Lebanese, boarding a Baghdad-bound bus in Beirut. “We are going to die. We know we will not come back,” says another, one of the 250 from Lebanon who are said to have volunteered for service in Iraq since the start of the war.

Few appear to be inspired by love for Saddam Hussein. “With our spirit and blood we will fight for Iraq,” chanted the Beirut bus passengers, pointedly altering a slogan that on Iraqi television, at least, usually runs “we will fight for Saddam”. Instead, the overriding motivation seems to be religious. With the blessing of Muslim clerics, including the Grand Mufti of Syria and scholars from Cairo's celebrated al-Azhar university, Iraq has been added to the list of legitimate zones for *jihad*.

“Iraq, we heed your call,” ran a communiqué from Islamic Jihad, a Palestinian extremist group responsible for dozens of suicide bombs against Israeli civilians. “It is one war from Najaf to Tulkarm and from Jenin to Baghdad.” The group says it has dispatched trained human bombs to Baghdad, and the Iraqi regime has already shown it is eager to use them. Its first suicide bomber, an Iraqi non-commissioned officer, killed four American soldiers at a checkpoint last week. Mr Hussein promptly rewarded his family with 100m dinars, worth $34,000.

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Humanitarian assistance

The other battle

Apr 3rd 2003
From The Economist print edition

Relief agencies face a daunting task

Get article background

AP

AS COALITION troops battle their way into Baghdad, relief agencies continue to give warning of a humanitarian disaster. On March 28th the United Nations launched an appeal for $2.2 billion, including $1.3 billion for food alone, to meet needs over the next six months. On the same day, the Security Council agreed to modify the oil-for-food programme (OFFP)—which allowed the Iraqi government to use part of its oil proceeds to buy humanitarian supplies under close supervision—to help the UN respond. Reluctant to be seen preparing for a conflict before diplomacy had run its course, foreign donors are only now announcing how much they are willing to spend.

Things were already grim for the Iraqis. Earlier wars and 12 years of sanctions had brought what used to be a middle-income country to its knees. In 1990 the United Nations Development Programme placed Iraq 76th in its human-development ranking; ten years later it had dropped to 126th, just ahead of Lesotho. According to Unicef, for every 1,000 children born in Iraq, 130 die before their fifth birthday (compared with 56 in 1984), mostly because of chronic malnutrition. GDP per head collapsed from over $3,000 in 1990 to around $700 towards the end of the decade. Even before the war started, Iraq had the highest number of internally displaced people in the region—about 1.1m.

Before the first bomb was dropped, 16m people—six Iraqis in ten—depended entirely on the OFFP for food. According to the UN, food rations made up 80% of the average income. Access to water is also a problem (see article): every day, some 500,000 tonnes of raw sewage are discharged into fresh water supplies. Sewage-pumping stations need power, and few have their own generators.

The OFFP was suspended on March 17th, and many humanitarian workers have left. Those still working in Iraq have only a partial picture. According to the International Committee for the Red Cross (ICRC), Baghdad hospitals caring for those hit by the bombing face no shortage of drugs as yet (they were stockpiled before the war started), and still have water and power. But this could change. In Basra, power cuts have threatened the supply of drinking water. The position in towns like Nasiriya, which have seen the fiercest fighting, is unknown.

So far, food supplies have been adequate. Before the OFFP was suspended, extra food was distributed to let people stock up (although some families have since had to sell these reserves). But the UN estimates that food will be running out by the end of this month. The Kurdish north, which received no extra rations of wheat flour before the conflict, may feel the pinch earlier; food prices there are soaring.

Iraqis have not yet fled to neighbouring countries. In the north, however, many Kurds left towns to seek refuge in the countryside when the fighting started, although they now seem to be going home. Some people also crossed from the area controlled by the Iraqi government to the Kurdish zone. Most of the displaced are cared for by relatives, which puts a heavy burden on their meagre resources. In Dahuk and Irbil, some of the displaced have sought refuge in schools.

If Iraqis start getting hungry and thirsty, or if the fighting intensifies in cities, the situation could get far worse. The UN High Commission for Refugees is helping Iraq's neighbours prepare for an influx of up to 600,000 Iraqis. Blankets, tarpaulins and other necessities are stocked in Turkey, Jordan and Iran, and

refugee camps are being prepared. The World Food Programme (WFP) has prepositioned enough food to feed 2m people for one month. After this it hopes to be able to feed the entire population for the next three months, using the 44,000 small shops in the OFFP network. This will be an operation four times bigger than the one in Afghanistan, and an unprecedented challenge for the agency.

Fresh supplies have started trickling in. On March 28th the British navy's *Sir Galahad*, carrying 230 tonnes of food, blankets and medicine, was finally able to dock at Umm Qasr after the waterway was cleared of mines. The next day, the WFP brought three trucks carrying 75 tonnes of dry milk into the north.

Who will pay for the relief effort? On March 28th the UN Security Council gave Kofi Annan, its secretary-general, the authority to adjust the OFFP, which used to be jointly managed with the Iraqi government. About $10 billion worth of supplies are in the pipeline, and the UN has designated more than 450 contracts for medicines, health supplies, food, water and sanitation, worth over $1 billion, as priorities for shipment. Some ask whether the OFFP is the right way to organise the effort: this was after all a partly punitive scheme, designed (and staffed at great cost) to deal with quite different circumstances.

Paying up

Donors have been opening their wallets, the United States among them. State Department agencies have spent more than $242m on Iraq—over $105m of it channelled through the UN and other international organisations—in addition to providing more than 600,000 tonnes of food. On March 25th George Bush asked Congress for $2.4 billion for relief and reconstruction, bringing the total to $3.5 billion so far. This is small compared with the $62.6 billion Mr Bush has requested for military spending in Iraq, but it is more than any other country has pledged.

Many humanitarian organisations have criticised the involvement of coalition troops. The laws of war put responsibility for the well-being of the civilian population on the occupying power, but relief organisations are wary of working with the military. According to Florian Westphal of ICRC, help for an area has to be based on need rather than on who is in control. To reach those in need, agencies have to work with both sides and must therefore remain neutral. In Basra, strict neutrality was essential to enable the ICRC to move between areas controlled by the Iraqis and those held by the coalition.

Christoph Wilcke of Save the Children, one of the largest NGOs operating in northern Iraq, also points out that humanitarian agencies are much better than soldiers at getting help to those who need it most. In southern Iraq, aid supplies have been mobbed by the strongest, leaving the vulnerable without.

This debate finds an echo within the American administration, where the respective roles of the State Department and the Pentagon in providing humanitarian assistance are blurry. The Agency for International Development, under the authority of the State Department, has put together the largest team it has ever assembled to help in Iraq. Now in Kuwait, it is supposed to co-ordinate American relief activities once the fighting stops. Nonetheless, an office for reconstruction and aid for Iraq (headed by retired Lt-General Jay Garner, also now in Kuwait) was created within the Pentagon in January. Uncertainty also surrounds the role of the UN, despite declarations from American officials that it would be “key”. Last week 14 big American aid agencies sent a letter to Mr Bush urging him to place the humanitarian effort in Iraq under UN auspices.

When the fighting and the debating stop, co-ordination will remain a mammoth task. The pre-war planning was fragmentary. Months of international debate over inspections and military intervention gave time to prepare, but the diplomatic split made it difficult for many organisations, notably the UN agencies, to gear up openly for the conflict and its aftermath. Most daunting is the sheer scale of the operation. In addition to its own and other official agencies, the UN has already listed 50 NGOs waiting in Amman, eager to go to Iraq once the country is safe. That may be just the start.

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Water

Lethal stuff

Apr 3rd 2003
From The Economist print edition

The war may do less damage to Iraq's water supply than sanctions did

AP

The silent request

Get article background

DIRTY water has killed vastly more Iraqi civilians than stray bombs and bullets. Engineers from the International Committee for the Red Cross have just helped to restart supplies in Basra—home to more than a million people—after an interruption of three days. But Iraqis have been dying in large numbers for years because of the long-term effects of economic sanctions on the water-supply infrastructure.

When sanctions were introduced in 1990, they were imposed on an economy that had been weakened by the Iran-Iraq war, then torn apart by the first Gulf war. Richard Garfield, a professor of public health at Columbia University, New York, says that after that first conflict with America and its allies, Baghdad was without a proper water supply for eight months. There was an outbreak of cholera. “Nobody cared, and the world turned away,” he says.

Sanctions caused serious additional damage to Iraq's water and sewerage infrastructure, as well as to the electricity-supply network that is crucial for pumping water across most of Iraq's flat landscape. Calculating the number of deaths caused by sanctions is both difficult and controversial, but Mr Garfield suggests that lack of infrastructure killed 20-40 people for every Iraqi who died during the first Gulf war.

Typhoid, as well as cholera, has reappeared; and that is no surprise. Around 500,000 tonnes of raw sewage are discharged every day into Iraq's rivers. In many unserved rural areas, people still fetch water for drinking and mix it with infant formula to feed their babies. Only one in three Iraqi women breast-feeds her baby in the first six months of life.

Whatever the precise figures, it is clear that Iraq has suffered a public-health disaster. And the root of the problem is simple. For the first five years of sanctions, Iraq was unable to import any of the parts needed to repair its water-supply system. Even after the oil-for-food programme started, it took another three or four years to replace damaged equipment because much of the gear could not be imported. Once the equipment was arriving, the main problem was people, says Mr Garfield. Iraq's water authority now has only half of the 10,000 staff it needs, and most of these are inexperienced. Engineers who could do so have either left the country or taken jobs that pay more—such as driving a taxi.

Despite the care that the allies say they are taking, the water-supply infrastructure in Baghdad and other towns is now at risk again. This time, at least, there will be no need for sanctions when the fighting is done.

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American diplomacy

Collateral damage

Apr 3rd 2003 | WASHINGTON, DC
From The Economist print edition

Gloom is settling on those who want to look beyond Iraq to repair America's relations with the rest of the world

OUR task, said Tony Blair delicately, is to work out “the diplomatic implications of recent events for the future.” He was speaking before his meeting last week with President George Bush at Camp David. But his words reflect a concern which goes beyond Britain: that the diplomatic crockery smashed before the Iraq war needs to be glued back together, for everyone's sake—and the sooner, the better.

The diplomatic costs of war in Iraq, at least in the view of the rest of the world, have been large. Relations with France and Germany, once two of America's closest allies, are barely cordial. For 50 years, Turkey too was one of America's most reliable partners. Now, Turkish peasants have taken to stoning American military vehicles, and America is moving its aircraft from Turkish bases to Kuwait.

Still more collateral damage has been done to America's relationship with Russia, which had been steadily growing warmer during Vladimir Putin's presidency. Mr Bush paid scant heed to Russian objections to an attack on Iraq. This has emboldened hardliners who have long argued that their country was not getting enough from improved ties with America (see article). Russia's parliament has refused to ratify a treaty cutting American and Russian nuclear arms by two-thirds.

Mr Blair is not alone in worrying about the implications of all this for international order and security. Others also seem to want to cool tempers. Gerhard Schröder, the German chancellor, last week said he thought “a sensible working relationship” with Mr Bush was still possible. He left open the chance that Germany might contribute financially to Iraqi reconstruction. Officials have hinted that Germany might also be willing to back a United Nations resolution endorsing an American-led transitional government in Iraq, so long as authority was handed over to the UN as soon as possible.

Even Jacques Chirac, the French president, has been downplaying his differences with Mr Bush. During the prolonged wrangling this spring within the UN Security Council, Mr Chirac became the Bush administration's nemesis. Now the French leader says that he, too, wants to avoid an adversarial relationship with the world's only superpower.

But is the Bush administration ready, or willing, to respond to these overtures? The answer to that question is still far from clear. On the positive side, it sent Colin Powell, the secretary of state, to Turkey this week, and he stopped off in Brussels on the way back for talks with NATO and European foreign ministers.

Mr Powell's trip mattered, if only because (like most administration members) he travels so rarely. Admittedly, the trip was partly to deal with the urgent problems of war, not the long-term health of the two countries' alliance. Mr Powell won agreement from the Turks to ship food, fuel and humanitarian aid across their border into northern Iraq, and he seems to have succeeded in restraining the Turks from invading Iraq themselves. By just travelling all the way to Turkey, Mr Powell pleased his hosts. And his visit came right after an administration request to Congress for $1 billion in fresh grants and loans to Turkey.

Repairing ties with Turkey should be relatively straightforward, because there is an obvious bargain to be made: a resumption of American support for Turkey over EU membership and over backing from the International Monetary Fund in exchange for Turkish co-operation during the war, especially in the sensitive task of dealing with the Kurds. It is not yet clear whether this bargain will stick. But here, at least, is a chance for America to piece together some of the crockery.

Two other issues present a much bigger challenge: the so-called “road map” for a resolution to the Israeli-Palestinian conflict and the question of who will run a post-Saddam Iraq. At his summit with Mr Blair, Mr Bush promised to publish the road map—a series of steps which America wants the Palestinians and Israelis to take to restart the peace process. This could, in theory, improve America's relationship with both the Arab states and Europe.

The trouble is that the map has already run into criticism from both parties who, though they have accepted it in general, want to make a dozen amendments. It seems unlikely that publication itself will change much. It is also unclear how much negotiations on the basis of the road map would improve American ties with the Arab world: the general Arab attitude is that the road map is a surrender imposed on a crippled Palestinian Authority. Moreover, any progress would require America to put real pressure on Israel. No one in the Bush administration has so far shown much stomach for this.

An equally big stumbling block to patching up relations with others will be the fraught question of who will run a post-Saddam Iraq. On March 28th, the Security Council voted to restart the UN's oil-for-food programme under Kofi Annan's authority. The programme had fed more than half of Iraq's population. To win agreement, the Americans dropped their insistence that the UN co-ordinate its relief efforts with the American military command in Iraq. Before that, at the Azores summit on the eve of war, Mr Bush said he wanted the UN to endorse the post-war interim government in Baghdad. That suggested he was willing to give others a role.

But what sort of role? Mr Blair wants the UN to be “centrally involved” in post-war Iraq. That does not seem to be what the administration intends. “We didn't take on this huge burden,” Mr Powell told Congress last week, “not to be able to have significant, dominating control.”

In short, the question of international involvement in the post-war settlement is open, at best. There are few signs that the Bush administration really wants others to participate in reconstruction and even fewer signs that others have accepted what the administration wants, an American-controlled interim authority.

Perhaps this impasse is temporary. The White House itself is entangled in a basic rule of politics—the immediate drives out the urgent. It is also worth pointing out that there was a stage in the Afghan conflict when no one knew who would run the interim government or where reconstruction money would come from. Suddenly Hamid Karzai appeared, and the Tokyo conference promised billions. As one senior official puts it: “We're not yet in a post-conflict situation. The most important thing is to win the war.”

That said, there are more daunting obstacles. The administration is divided, as usual. The State Department wants to mend the crockery. Diplomats apply the term “post-war reconstruction” to America's broken alliances, not just Iraq. But two groups within the administration oppose them. One group says it is too early for diplomacy. The outcome of the Iraq war will fix automatically most of the difficulties, it claims. Engaging in diplomatic processes for their own sake is foolish. The other group, more brutally, wants revenge. Mr Bush's White House believes fervently in loyalty—and Messrs Chirac and Schröder are regarded as disloyal.

Worryingly, neither of these two groups accepts what is so evident abroad: that war in Iraq has caused

significant damage to American interests. They see the conflict through the prism of the Anti-Ballistic Missile treaty and the Kosovo and Afghan wars. In each case, they argue, America took a decision, others complained bitterly, but then later endorsed the outcome. Two weeks of combat, after a failure to win a second UN resolution, have not been enough to change their minds. Until that happens, Mr Bush seems unlikely to follow Mr Blair in investing real political capital in the transatlantic alliance. Those hoping for a big American diplomatic effort may be waiting in vain.

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Budget politics

Mushy moderates

Apr 3rd 2003 | WASHINGTON, DC
From The Economist print edition

Republican moderates have clout. They just don't know how to use it

MODERATE Republicans have been a political species long reputed to be close to extinction. But reports of their death seem to have been greatly exaggerated. In recent weeks they have been causing a commotion on Capitol Hill. Their defections in the Senate defeated the Bush administration's latest attempt to permit oil drilling in Alaska's wildlife reserve and halved the size of George Bush's tax cut from $726 billion over ten years to $350 billion. Even in the more conservative, and more disciplined House of Representatives, opposition from moderates forced House leaders to modify the spending cuts in their budget proposals. Do these victories mean centrist Republicans are becoming a serious political force, capable of undermining Mr Bush's domestic agenda?

Probably not. In the House of Representatives, the number of moderate Republicans is small and the number willing to take on the Bush administration publicly is smaller still. This is especially true when it comes to top priorities, such as tax cuts. Tom Mann, a political analyst at the Brookings Institution, reckons that around 30 House Republicans would prefer no new tax cuts. And yet far fewer than this number raised any objections at all publicly and only 12 actually voted against the budget resolution.

What explains the moderates' timidity? Party leadership plays a big role. The Republican machine in the House is one of the most effective in decades. The White House, too, has a formidable reputation for not forgiving, or forgetting, dissent. From lobbyists to congressmen, the refrain is that you cross “team Bush” at your peril. Fear of challengers at the polls also muzzles centrists, particularly since conservative activists founded the Club for Growth, a political group whose explicit goal is to support conservative tax-cutting candidates to challenge moderate Republicans in primaries.

In the traditionally more independent Senate, Republicans' willingness to disagree with their leaders is greater. And given the tiny Republican majority, the half dozen centrist Republican senators wield enormous potential power. Just three defections were enough to halve the tax-cut plan. However, centrist Republican senators are more a collection of unpredictable individualists than a coherent political grouping, and this has weakened their clout.

John McCain, chief Republican maverick, has argued loudly, and firmly, against any tax cuts. He even voted against the $350 billion figure. Lincoln Chafee, a Rhode Island senator, claims to be against any tax cuts but voted in favour of the $350 billion. Olympia Snowe, a moderate from Maine, and George Voinovich, a fiscal hawk from Ohio, were pivotal votes for slimming the size of the cut. But both have already hinted that they could live with a bigger tax cut when the final package is hammered out between the House and Senate. And both are under extraordinary pressure from the White House.

Other moderates have already caved in to the administration. Arlen Specter, a centrist from Pennsylvania, voted for Mr Bush's budget plans, even though he initially voted against the 2001 tax cut, preferring instead to spend more money on education. (It is no coincidence that he faces a tough primary challenge from a conservative financed by the Club for Growth.)

Given the moderates' inability to stick together, it is not surprising that both the White House and Republican congressional leaders are confident that the final tax-cut figure will be much higher than $350 billion. The most conservative congressmen, who are much better at lobbying as a group, are threatening to oppose a smaller cut. Although the haggling is likely to continue for several more days, there is talk of a compromise figure between $500 billion and $600 billion. That would be enough to accelerate all the reductions in income tax that Mr Bush's 2001 cut introduced gradually, and to leave room for reducing by half the taxation of dividends, though not eliminate it, as the White House wants. This is not quite as much as Mr Bush asked for. But with deficits stretching as far as the eye can see, it is still, according to

your point of view, either pretty bold or pretty reckless.

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Affirmative action

It is so ordered

Apr 3rd 2003
From The Economist print edition

The Supreme Court wrestles with racial preferences

Get article background

WHOEVER chose April 1st as the day for oral arguments before America's Supreme Court on two affirmative-action cases must have had a sense of humour. The task of resolving America's heated debate about the use of racial preferences in university admissions looks, indeed, like something of a fool's errand. Whatever the court decides, it seems bound to leave plenty of people unhappy.

Of course, the court's nine justices have often handed down unpopular decisions. And they are used to ignoring the kind of noisy protests outside their building which occurred this week. But unless they can fashion a solution widely viewed as fair, their ruling could inflame passions on both sides and leave the nation's universities wrestling with an even more intractable problem than they faced after the court's last ruling on the issue 25 years ago.

Righting past wrongs towards African-Americans is no longer the prime rationale for affirmative action, at least in university admissions. Current affirmative-action policies—which now usually include Hispanics as well as African-Americans—aim to maintain racial diversity, which America's top universities argue is an educational priority. Diversity helps to break down racial stereotypes, they say, and equips all students to become leaders of a multi-ethnic country by exposing them to a broad range of views. The bald but unfortunate fact is that if race were not taken into account, few blacks or Hispanics would win admission to top universities or law and medical schools based on grades or test scores alone.

Polls show widespread support for the idea of diversity, among students as well as the general public. On the other hand, polls also show growing resentment among whites and Asian-Americans at the admission of less-qualified blacks and Hispanics to elite institutions, where competition for places can be fierce. There are also growing calls for a return to the ideal which first launched America's civil-rights movement—that no one should be judged by the colour of their skin.

The two cases before the court this week have been brought against the University of Michigan and its law school by white students who claim that they were unfairly denied admission. They argue that this is contrary to fundamental guarantees of equality in the constitution's Fourteenth Amendment as well as the 1964 Civil Rights Act.

The two cases have attracted enormous attention. A record number of “friends of the court” briefs have been submitted to the court. In January George Bush, following a tense debate within his administration, ordered the solicitor-general to file a brief on the side of the students and spoke personally against the university's admissions policies.

Supporting Michigan are many other leading universities, both public and private, as well as hundreds of large companies, state governments, trade unions, professional associations, and former military leaders. This broad coalition backs the diversity goal of current affirmative-action policies and does not want to see them abolished. And yet the diversity exception to anti-discrimination rules rests on a remarkably shaky legal foundation.

Diversity was first endorsed by the Supreme Court in its 1978 *Bakke* decision. Although that decision became a landmark, it was one of the most fractious and complicated in the court's history, with the nine justices picking apart each other's published opinions and dissents, paragraph by paragraph.

The late Justice Lewis Powell wrote for a five-vote majority, ruling out a specific racial quota to ensure

that enough African-Americans were admitted to the University of California's medical school. Oddly, Powell's opinion also sided with the other four justices ruling that, although numerical quotas were illegal, race could be taken into account in admitting students, but only as one of many other factors. For Powell, racial “diversity” was a “compelling state interest” which allowed an exception to the Fourteenth Amendment's general stricture against racial discrimination, but only if the method used was “precisely tailored” to that goal. But some of the other justices supporting affirmative action wrote yet more opinions, sticking with the earlier rationale that affirmative-action policies were justified as a remedy for past discrimination. Powell alone seemed to lay the entire weight of his support for racial preferences on “diversity”.

For those hoping that the court will now overrule *Bakke* and sweep aside affirmative action as anachronistic and unfair, the Bush administration's brief was a disappointment. The result of a political fudge, the brief endorses the University of Michigan's goal of racial diversity, and only quarrels with its complex system of awarding “points” to minority applicants as, in effect, a disguised and illegal quota. Instead, the Bush administration argues that other “race neutral” forms of admission can achieve similar results and points to, among others, Mr Bush's home state of Texas, where the top 10% of students from all of the state's high schools are admitted to the University of Texas.

Critics say this is disingenuous. Such an approach produces racial diversity at the university level only because of racial segregation among high schools, and it continues to discriminate against better students at some schools in favour of duller ones at others. Moreover, it will fail in many states with different patterns of segregation, or for private universities and law or medical schools, which accept students from across the nation. The administration, on this view, is asking the court to tinker yet again with racial preferences to make them less objectionable, not to scrap them altogether.

Tinkering, in fact, is what the court seems most likely to do. Observers expect it to be split down the middle, with the “swing” justice, as in so many other cases, being Sandra Day O'Connor. As the first woman ever appointed to the court, Justice O'Connor is herself a beneficiary of affirmative action of a different sort, and she praised the benefits of gender diversity in a new book. Her sceptical questions at the oral hearing this week did not bode well for affirmative action's opponents. On the bench, she has been an incrementalist, and is usually reluctant to endorse the direct overturning of precedents as important as *Bakke*.

The court does sometimes spring surprises. And yet, even if it unexpectedly rules out all affirmative-action policies, that may not be the end of the matter. Top universities are unlikely to abandon their attempts to recruit minority students and will probably pursue them through various “outreach” programmes in high schools. These too could become the target of lawsuits, as could other factors aside from race used by university administrators to shape their student bodies, such as geography, gender and the so-called “legacy” preference—the extra consideration given to the children of alumni or contributors.

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Arts funding

Penny pinching

Apr 3rd 2003
From The Economist print edition

Arts organisations across the country are running out of cash

“IN ART, economy is always beauty,” wrote Henry James. America's beleaguered museum and opera-house directors must hope that he was right. Across America, hard times have left arts budgets in sorry shape. The Metropolitan Museum is grappling with a $5m deficit this fiscal year, with a further gap of $8m projected for next year. The Pittsburgh Symphony is $2m in the red. Symphonies in Colorado Springs and San Jose have gone bankrupt, and the Houston Symphony, also in the red, was hit by a musicians' strike last month.

Falling donations are much to blame. In 2001 charitable contributions to the arts, culture and humanities reached $12 billion—or 5.7% of all American philanthropy, according to *Giving USA*, a publication which tracks charitable contributions. Since then donors, battered by declining stockmarkets, have been closing their wallets. Stockmarket falls have also reduced income from endowments, and shrinking profits have hurt donations from companies. Many foundations have shifted their attention away from the arts to other worthy causes, such as vaccination and education, reports Andras Szanto, deputy director of the National Arts Journalism Programme at Columbia University.

The squeeze on overall state budgets has made things still worse. California and Massachusetts chopped arts spending by half and 62% respectively in fiscal 2002-03, and across the nation state-spending on the arts fell 13.4%, according to the National Assembly of State Arts Agencies. Colorado, New Jersey, Arizona and Missouri are talking of eliminating their state arts councils, which distribute grants to artists. Some cities too are trimming: in New York, Michael Bloomberg, the mayor, cut arts funding by 6% this year. Deeper cuts are probably on the way.

Another headache is falling visitor numbers. Around 20% of all arts funding comes from ticket sales; still more from spending in gift shops and cafés. But tourism is down since the September 11th terrorist attacks. Attendance at the San Francisco Museum of Modern Art has fallen 13% since 1999. War in Iraq this year is unlikely to help revive visitor numbers.

To stop from falling too far into the red, museums and operas are cutting performances and opening hours (the San Francisco Opera will have a quarter fewer productions by 2005-06). Staff too are being laid off, or taking pay cuts. Musicians at the San Antonio Symphony have even played without pay.

This penny-pinching hurts all the more because it mocks the big expansions undertaken in the 1990s. Now, says Mr Szanto, some snazzy new buildings are understaffed or filled with thinner programming. The brashest of these efforts was the Guggenheim, which was forced to close part of its Las Vegas branch in January, barely a year after it opened. Plans for a second New York City Guggenheim have also been shelved. Undaunted, the Guggenheim is in negotiations about opening a new branch in Rio de Janeiro. The local government is supposed to provide the money. Given Brazil's own budget problems, this seems optimistic. Other museums have abandoned their expansion plans. Last December the Los Angeles County Museum of Art postponed plans for a fancy renovation and expansion that could have cost over $200m.

Amid the wreckage, a few museums are moving boldly ahead. The Museum of Modern Art in New York began a big renovation last year, which is due to be finished in 2005. The Kennedy Centre in Washington, DC, is embarking on a $650m project that will bring an elaborate new plaza and buildings. But $400m of this (the cost of reworking the adjoining mess of roads) will be paid for by the federal government. Arts organisations outside the nation's capital have not been so lucky.

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Lexington

Tough enough

Apr 3rd 2003
From The Economist print edition

George Bush possesses the most important quality of a war leader—determination

Get article background

GEORGE BUSH could hardly have worse qualifications for the job of war leader. He wriggled out of serving in Vietnam, ran for the presidency promising to keep America out of foreign entanglements, and enjoys a rocky relationship with a resource that Winston Churchill regarded as more important than bombs and bullets: the English language.

But just look at him now. The frat boy president is leading America in one of the most divisive wars in decades, a war that has strained long-standing alliances, inflamed the Arab street and alienated a fifth of the American population. How is he doing? Is he growing in stature? Or is war finally exposing his limits as a leader?

Two weeks into the war, he has already established a clear leadership style. Mr Bush's fellow Texan, Lyndon Johnson, shoved his nose into the smallest details of the Vietnam war. He chose bombing targets, visited the war zone and appeared on television so often that the war looked like a personal crusade. At one low point during the conflict, he even had a scale model of the battlefield constructed in the White House so that he could play military commander.

Mr Bush is much less hands-on. You cannot quite accuse him of being above the fray. He personally took the decision to kick-start the war with a missile attack on Saddam's headquarters. He has forcefully backed his defence secretary, Donald Rumsfeld, in the growing argument about whether Mr Rumsfeld's war plan puts too few boots on the ground. He makes regular public appearances with soldiers in uniform. The White House is well aware that, back during the Iranian hostage crisis, Jimmy Carter lost his emotional bond with the American people because he made so few public appearances.

But Mr Bush shows a firm grasp of the principle that less can be more. He is being careful to avoid second-guessing his cabinet ministers or micro-managing his troops. (One interfering civilian, in the form of Mr Rumsfeld, is more than enough.) He is being equally careful not to personalise the conflict with a man who has tried to kill his father.

So far this style is going down pretty well. The latest Gallup poll shows that 71% of Americans approve of

his job performance. But Mr Bush has to negotiate three pitfalls if he is going to keep the momentum in the coming months.

The first is that he is such a polarising figure—a divider rather than a uniter. Mr Bush's “bounce” in the opinion polls from the war has been relatively small—about ten points rather than the 26 points that his father enjoyed. America has entered what could be a protracted war with a good chunk of its own population firmly set against the enterprise. Tony Blair has managed to persuade a surprising number of people in Britain, thanks to the sheer force of his intellect and conviction. Mr Bush has succeeded only in reinforcing entrenched attitudes.

The second weakness is that he is trying to advance on the domestic as well as the military front. Mr Bush is determined not to repeat his father's mistake of winning the war in the Gulf but losing people's confidence at home. But this is easier said than done, particularly given his highly partisan agenda. Mr Bush is encountering stiff resistance on Capitol Hill from both Democratic snipers and Republican turncoats. In the past few weeks the Senate has halved his tax cuts and shot down his plans for drilling in Alaska.

The third is his famously twisted tongue. Some of his recent off-the-cuff performances have been painful to watch. In the Azores he sounded as if he were recovering from a lobotomy. His press conference on March 6th was a canned affair: a repetition of familiar mantras rather than a genuine attempt to advance arguments or engage with criticism.

But none of this will necessarily do him much harm, short of a complete military debacle. The American public had no illusions that war with Iraq would be a cakewalk. Far more Americans think that the war will last for more than a year (14%) than think that it will be over in less than a month (6%). More than a quarter think it will last for up to six months. The more the Iraqis resort to suicide bombings and talk of taking the *jihad* to America, the more they confirm the administration's argument that Saddam Hussein and Osama bin Laden are twin faces of the same evil.

Mr Bush has a reasonable chance of covering his flank on the domestic front, snipers or no. If he succeeds in passing his tax cuts, he will galvanise his Republican base; if he fails to get them through, he can always blame the Democrats. Even Mr Bush's ability to drive his critics nuts may prove to be a godsend. Every time that America hears from the likes of Michael Moore, a film maker who turned the Oscar ceremony into an excuse for Bush-bashing, Mr Bush strengthens his hold over the mainstream.

And is Mr Bush's twisted tongue really as important as journalists imagine? At first, even Abraham Lincoln was widely regarded as a tongue-tied country bumpkin. Dwight Eisenhower was famously inarticulate. George Bush is capable of delivering fine set-piece speeches (though no one believes he will ever come up with a Gettysburg address). He is also a master at pressing the flesh with military people, something that he will have to do often in the coming weeks.

Mr Bush's obvious weaknesses are more than offset by his biggest strength: dogged determination. So far his presidency has been a study in stubbornness—in setting clear goals and pursuing them regardless of the costs or consequences. His two favourite war leaders, Churchill and Lincoln, were both models of stubbornness. This stubbornness helps to explain why Mr Bush enjoys such high levels of trust from Americans. It also explains why so many foreigners fear that he is quite prepared to shake the world to its very foundations.

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Reforming Brazil

Lula's great pension battle

Apr 3rd 2003 | SÃO PAULO
From The Economist print edition

The government prepares to unveil two all-important reforms

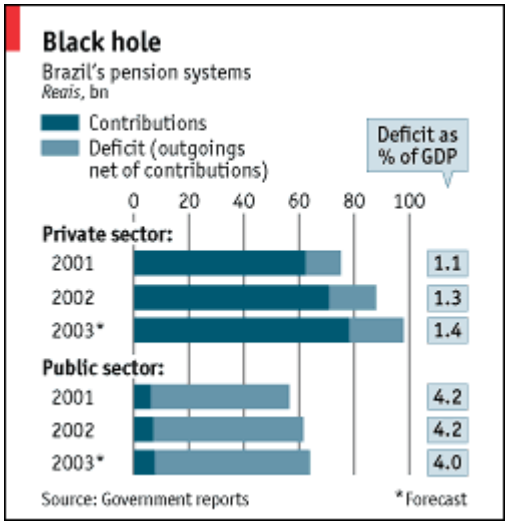
Get article background

HE HAS spent his first 100 days plotting strategy and marshalling forces. Now Luiz Inácio Lula da Silva, who took office as Brazil's president on January 1st, looks poised to strike. “When you're in opposition, you can strut about because you don't have to manage anything,” a feisty Mr da Silva told businessmen in São Paulo last week. “Now that we're in government we have to act.” By that he means sending the two proposals that could make or break his presidency—for reforms of pensions and the tax system—to Congress this month. He wants to deliver them on foot, marching at the head of a column formed by Brazil's 27 state governors.

A complex and burdensome tax code and a wasteful and money-losing pension system are two of the main reasons for Brazil's slow economic growth and notorious inequality. But they benefit powerful groups. Persuading Congress to change them will be a long slog. The government's first big legislative victory, on April 2nd, may set the pattern. The lower house of Congress voted for a constitutional amendment to pave the way for granting autonomy to the Central Bank, overcoming resistance from radicals within Lula's own Workers' Party (PT). But the dissidents extracted a price: the government will not introduce a bill to grant the bank autonomy without further consultations.

The government's most urgent task is to reform the pension scheme for civil servants, which is an affront to equity as well as fiscal responsibility (see chart). It is not mere arithmetical coincidence that the public-sector pension system, which benefits only 2.5m Brazilians, runs a deficit just shy of the budget surplus (before interest payments) of 4.25% of GDP which the government must maintain to stabilise the public debt, and which constrains its spending on the poor. By contrast, the publicly-administered scheme for private-sector pensioners helps 20m people and has a deficit of just 1.3% of GDP, though this, too, is growing.

Brazil's government pensions are “the most generous in the world”, says Flávio Rabelo of the Fundação Getulio Vargas, a business school in São Paulo. Civil servants do not merely retire on full salary; they get, in effect, a pay rise because they stop paying contributions into the system. Most women retire from government service at around 50 and men soon afterwards. A soldier's widow inherits his pension, and bequeaths it to her daughters.



Lula intends to trim rather than chop. The government is expected to propose five main changes:

• Raising the minimum age for retirement by seven years (to 60 for men and to 55 for women).

• Doubling, to 20 years, the time people must work in government to qualify for a civil-service pension.

• Obliging future retirees to continue to pay pension contributions.

• Reducing the benefits of widows and other dependants to 70% of the original pension (and cutting off soldiers' daughters at 21).

• Subjecting newly-hired civil servants to a regime similar to that for private-sector workers. This caps pensions (at 1,561 *reais*, or $465, a month); they can be topped up by voluntary schemes.

With all of this, the federal government expects to save 1.7 billion *reais* next year—the cost of Lula's pet Zero Hunger anti-poverty programme. To this should be added savings by state and municipal governments, and in military and other special pension schemes. Overall, guesses Alexandre Marinis of CSFB, an investment bank, in its first year the reform would yield savings of 0.5% of GDP at most.

That would be helpful, but not earth-shaking. Lula could raise an extra 4 billion *reais* a year by levying a tax on existing pensioners, but seems reluctant to tussle with the Supreme Court over the issue. He could also break the link between salaries and pensions. This makes it prohibitively expensive to reward workers properly, points out José Cechin, a former social-security minister. But Lula's proposal is unlikely to tackle this.

Caution does not guarantee smooth passage. A group of public-sector unions, most linked to the PT, plans a one-day protest strike on April 8th. The head of the university professors' union spoke of his members' “feeling of betrayal, of revolt”. Mr da Silva is unfazed. He says he will “confront” opposition from within the ranks of his own supporters.

The president's governing alliance lacks a majority in Congress. He hopes to rectify this by bringing in the Party of the Brazilian Democratic Movement, a large centrist group, but that may not happen soon. Opposition parties support reforms in principle, but have little incentive to make life easy for a president whose party opposed those self-same reforms when they were in power.

The betting is that Congress will approve modest and piecemeal changes to pensions this year. The same may even go for tax, where the government's main wish is to unify a patchwork of state value-added taxes. In each case, this would amount to less than total victory for Lula, but it would be progress, of a sort.

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Corruption in Chile

Losing its shine

Apr 3rd 2003 | SANTIAGO
From The Economist print edition

What is going wrong in Chile?

Get article background

FINANCIAL markets and politicians alike shrugged off the resignation this week of Carlos Massad, the president of Chile's central bank. But the fraud that caused his downfall has tarnished the country's reputation for financial probity.

Mr Massad, who was only a few months into a second five-year term, did nothing wrong himself. But early in February, he discovered that his secretary had been selling market-sensitive information to Inverlink, a local financial group. The news triggered Inverlink's collapse, as savers yanked their money from its mutual funds. That in turn uncovered another scam: Inverlink had also been bribing an employee at Corfo, the state economic-development agency, to “lend” it certificates of deposit (CDs) as collateral for short-term operations in which it cashed in on its inside information. To raise funds to cover withdrawals, it began selling these CDs. Over $100m-worth were sold to mutual funds and other local institutions before Corfo discovered the theft.

The Inverlink affair has undermined public confidence in mutual funds: in March, savers withdrew $1.5 billion, or a quarter of the industry's total assets. And the secondary market in CDs has stalled, pending new procedures for verifying their ownership. To make matters worse, the government at first insisted that the mutual funds, rather than Corfo, should pay the bill.

All of this follows two other scandals. Bribes were paid at the Transport Ministry. And the Public Works Ministry used irregular payments from contractors to top up officials' salaries, and perhaps to fund political parties. The amounts involved are relatively small. It reflects well on Chile that they have caused so much fuss, and are being investigated. Even so, they have dented its claim to differ from its neighbours in being squeaky clean. “Now we know Chileans are human after all,” notes Arturo Porzecanski, who follows emerging markets for ABN-Amro, a Dutch bank.

So far, the scandals do not appear to have deterred foreign investors, nor dented President Ricardo Lagos's public standing. But his government now has the job of restoring confidence by improving the regulation of financial markets and of the public administration.

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Gambling in Mexico

Vegas, south and by the sea

Apr 3rd 2003 | MEXICO CITY
From The Economist print edition

A battle to bring casinos to Mexico

RECENTLY tarted up, and packed on race days, Mexico City's enormous Hipódromo looks like the shining jewel in a thriving gambling industry. Not so: under a 1947 law, Mexico banned all forms of gambling, unless explicitly authorised by the federal government. And the government has handed out permits only to the racecourse, and to a few chains of off-course bookies.

For the past few years, legislators have tried to overturn the gambling ban, one of the strictest in the Americas. A majority in Congress is thought to be in favour of allowing casinos across the country. Now, supporters are trying to hammer out a legislative proposal before Congress goes into recess in July. But they are running into resistance.

The champions of casinos offer a vision: of turning Mexico's holiday resorts, such as Cancun, Los Cabos or Puerto Vallarta, into Las Vegas-by-the-sea. Salvador Cosío, of the formerly ruling Institutional Revolutionary Party (PRI), who comes from Puerto Vallarta, points out that Mexico's tourist industry is highly seasonal: only one hotel room in two is taken in the slow months between April and December. He reckons casinos would provide a year-round attraction for Americans and Europeans. The government agrees: it estimates that casinos could stimulate a 30% rise in foreign tourists, most of them from the United States. After all, runs the argument, you can take in a fake Paris or Venice after clearing the tables in Vegas, but you cannot then go and roast on a real beach.

Mr Cosío stresses the benefits: a plan for an $80m casino in Puerto Vallarta owned by local authorities in partnership with Quebec's provincial government would generate not just 1,700 jobs but extra government revenues. But he faces a hard sell. Many Mexicans think of gambling as being linked to drug-trafficking and organised crime. The 1947 law was a response to the sordid reputation of the casinos opened along the frontier with the United States in the 1920s and 1930s.

Opponents play on that reputation. Casinos would become centres for laundering drug money, argues Daniel Olivares, who heads a pressure-group that supports the ban. He has allies in the leftish Party of the Democratic Revolution, who worry that in a country where 40% are poor, many are vulnerable to addictions of any kind, including gambling. So the gambling lobby may have the numbers in Congress, but the dice could still be loaded against change.

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Argentina's economy

Poised for growth?

Apr 3rd 2003 | BUENOS AIRES
From The Economist print edition

The Duhalde government has achieved more than its critics allow, but less than it might have

Get article background

ARGENTINA passed another milestone last week on its long, hard road back from economic collapse. Roberto Lavagna, the economy minister, announced a four-month timetable for lifting the last remaining controls on bank savings, affecting $4.8 billion in deposits. Although a third of this sum will be repaid in government bonds (if Congress approves), for the first time since late 2001 Argentines will have free access to their savings. The central bank has also announced a further easing of the capital controls imposed last year and this week it revealed a plan to buy back most of the outstanding scrip (funny money) issued by cash-strapped provinces.

These measures follow many other signs of incipient recovery in Argentina. The peso has appreciated steadily (see chart). Inflation, after surging a year ago, has subsided. Mr Lavagna reckons that the economy will grow by more than 4% this year. By the ugly expedient of threatening to default on its loans to official creditors, the government in January extracted a temporary agreement from the IMF, despite bitter opposition from the Fund's staff. Thanks to all of this, the next president, who is due to take office on May 25th after an election this month, will enjoy a better inheritance than the past two—or so Mr Lavagna contends.

President Eduardo Duhalde—installed by Congress in January 2002 after his predecessor resigned—and his officials argue that they have hauled Argentina out of its deep hole, but been given little credit for it. That is partly true. Largely unnoticed at the time by outsiders, Mr Lavagna began in mid-2002 to get a grip on fiscal and monetary policy. That halted inflation, and the free-fall of the peso and the economy. At the same time, the devaluation of January 2002, chaotic though it was, has started to do its work: exports are growing, and local products are being substituted for imports. Farmers are doing well: this year's harvest is close to a record. Factories are no longer being closed; indeed, some industries, such as textiles, which could not compete under the previous fixed exchange rate, are starting to revive. Tourism is booming: foreigners are flocking to Patagonia. As newly-poor Argentines stayed at home, the country's Atlantic resorts had their best summer since 1992.

Two big criticisms are made of Mr Duhalde's record. The first concerns his initial bungling of the devaluation, in which bank deposits and loans were converted by diktat to pesos at different rates. The second concerns what his team has not done.

Four big obstacles still block the road to sustained economic growth. The first is the public debt. Argentina defaulted on roughly $60 billion in bonds in December 2001. However, since then, the government has issued (or announced) new bonds totalling $27 billion, mainly to compensate banks and savers for the conversion to pesos. But it has yet to start talks on restructuring its debt. Since almost 700,000 creditors in seven different legal jurisdictions are involved, these talks will be long and difficult. And it is hard for Argentina's companies to renegotiate their debts until the government has done so.

Second, even if the government persuades creditors to accept a write-down of 70% of the value of the defaulted bonds, if it is to service its other debts it must generate a primary fiscal surplus (ie, before interest payments) of 4-5% of GDP, reckons Miguel Broda, an economic consultant. That is something

Argentina has rarely managed in living memory.

A start has been made. The government has resisted pressure to raise public-sector wages, whose real value has been savaged by inflation. Last year, provincial governments managed a small primary surplus. So far this year, the government is meeting the fiscal targets agreed on with the IMF. A senior official argues that from next year, growth and a stronger peso mean that a primary surplus of 3% of GDP would be both achievable and sufficient to pay the debt. But, he notes, holding spending down will be more difficult as the economy recovers. And tricky reforms of tax and provincial finance are needed.

The third problem is a banking system that is both insolvent and too large for a shrunken economy. Mr Broda points out that 56% of the banking system's assets consist of paper from a government that is in default. Only about half of the banks' private-sector loans are up to date. Several foreign banks have pulled out, though others remain. Before a smaller, stronger system can emerge, a new banking law and tougher regulation are needed.

Fourth, the devaluation involved widespread repudiation of contracts. The IMF worries, for example, that by granting only modest rises in the tariffs of privatised utilities, Mr Duhalde is storing up inflation for the future. Utility companies have debts totalling $45 billion. But they also know that many of their customers cannot afford big tariff increases, so the IMF's concerns may be overblown. A more tangible obstacle to future investment is a corrupt and politicised judiciary.

Until these problems are resolved, Argentina's recovery must rely on cash, not credit from local banks. For a while, that may be enough. Argentines hold some $100 billion in cash or in foreign banks. Thanks to the investment of the 1990s, much of the country's machinery and infrastructure is fairly new. But there is an urgent need for export finance, says Jorge Forteza, of Booz Allen & Hamilton, a management consultancy. He sums up the new government's main task as being to rebuild Argentina's financial and economic links with the world.

To do so, it faces a tight timetable. Apart from the debt talks, its first job will be to negotiate a medium-term agreement with the IMF; the current one lapses in August. Mr Duhalde will indeed leave Argentina in a much better state than he found it—but he is also bequeathing many unpopular decisions to his successor.

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SARS

After the outbreak

Apr 3rd 2003 | BEIJING AND HONG KONG
From The Economist print edition

Getty images

Even as the epidemic appears to stabilise in Hanoi and Singapore, Hong Kong, its centre, is a changed city

AT DAWN on March 31st, police wearing surgical masks, gloves and cloaks cordoned off Block E of Amoy Gardens, a housing estate in Hong Kong, and placed all those inside under quarantine. But only 241 tenants in 108 flats were left. The residents of the other 156 flats had already fled—to relations, hotels or friends—possibly spreading the virus they were suspected of carrying with them into the community. Amoy Gardens and much of Hong Kong recalled pestilent Oran, in Camus's "The Plague": "And while a good many people adapted themselves to confinement and carried on their humdrum lives as before, there were others who rebelled and whose one idea now was to break loose from the prison-house."

The outbreak at Amoy Gardens of SARS—Severe Acute Respiratory Syndrome—a new and barely understood type of pneumonia, may mark a turning-point in the global epidemic. Since it entered Hong Kong from southern China in February, SARS has spread to at least 16 other countries. Besides China itself, which remains tight-lipped about the true extent of its outbreak, Hong Kong is the worst-hit city, followed by Singapore. At mid-week, more than 2,200 people had been infected worldwide—over 700 of them in Hong Kong—and 78 had died.

Until last weekend, virtually all the infections could be traced to direct contact with a person showing symptoms of the disease (high fever and a dry cough). At Amoy Gardens, over 200 people went down with SARS in a matter of days, and their only link was that they lived in the same group of buildings, often vertically above or below one another. This raised the possibility that transmission might occur not only through droplets expelled by coughing, but through air-conditioning systems, water pipes or contaminated surfaces such as lift buttons.

For Hong Kong's government, Amoy Gardens was the signal that a genuine crisis was at hand. In the preceding three weeks, as new cases had been appearing at a rate of 20, then 50 a day (and even as the head of Hong Kong's hospital authority himself contracted the virus), it had still played down the risks. Its approach contrasted especially with the much faster and more drastic—some say draconian—response by Singapore, which almost immediately closed all schools and put 1,000 people under quarantine. Now, with some 80 new cases a day, Hong Kong's schools are closed too. A quarantine law not used since an outbreak of bubonic plague in 1894 has been invoked, and the remaining residents of Amoy Gardens are being sent to confinement camps.

Ordinary life in Hong Kong has changed beyond recognition. Restaurants are empty. Supermarkets are

full, as people stock up with rice, instant noodles, lavatory paper and disinfectant. An unfounded rumour that Hong Kong as a whole might be quarantined led to panic buying. Streets in the business district, normally bustling, are eerily quiet. Rush hour is gone, as people try to take public transport at unusual hours. Everybody who has a face mask wears it. Others are having masks sent express from abroad, as the city's chemists have been out of supplies for weeks. Concerts are cancelled. Whenever people do meet—masked, invariably—a surreal mixture of anxiety and denial hangs in the air.

The economic disruption is severe. HSBC, the city's main bank, had to close a floor of its main office after an employee showed symptoms. It also sent 50 traders home for a week as a precaution, and is preparing a back-up dealing floor. Other companies that have evacuated staff after suspicious cases include PCCW, Hong Kong's dominant telecoms provider, and Hewlett-Packard and Intel, two American technology giants. Everybody who can work from home does so.

Tourism, 5% of Hong Kong's economy, had virtually stopped even before the World Health Organisation (WHO) and America's State Department advised people not to visit. Inbound business travel has slowed to a trickle. Hotels are largely empty. After several sufferers were spotted on aircraft, Cathay Pacific, the territory's main airline, reduced its regional flight schedule, as have Singapore Airlines, Australia's Qantas, Air New Zealand and other carriers (see article). The Hong Kong stockmarket has fallen to a four-and-a-half-year low, and some economists are predicting a renewed recession.

Simmering beneath the worries is anger at mainland China, and especially at neighbouring Guangdong, the province with which Hong Kong during normal times claims to be working well on everything from economic integration to fighting crime. Guangdong had an outbreak of pneumonia, now proved to be SARS, as long ago as last November. But instead of providing information to the WHO, the government in Beijing stayed silent for months and ordered the Chinese media to avoid the subject. It now admits to 1,190 cases, 1,153 of them in Guangdong, and has at last allowed a visiting team of WHO experts to travel to Guangdong. But the daily updates it has been promising have not begun yet.

China has a long history of obfuscation. It covered up the spread of HIV in Henan and other provinces, and it routinely lies about economic and other statistics. Yet China, especially its crowded southern provinces, is also a breeding ground for new diseases—several global influenza epidemics of the past century, including the one that killed tens of millions in 1918-19, are thought to have originated there. The death rate from SARS is only 4%. What is the world to do when China is slow to share information about the next, perhaps deadlier, bug it produces?

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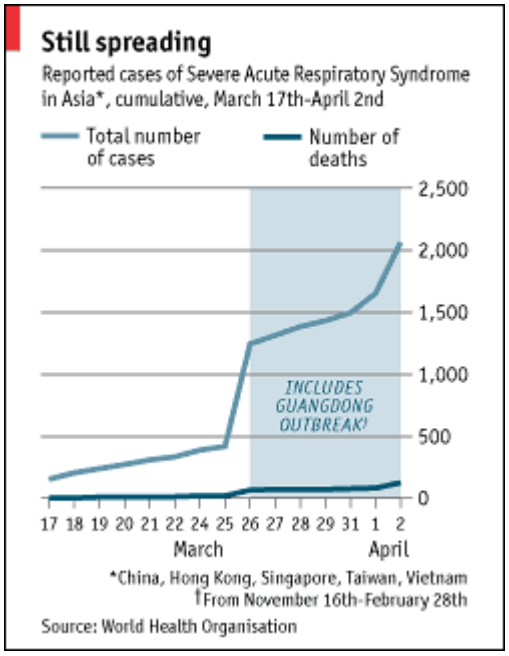
The science of SARS

A deadly mystery

Apr 3rd 2003
From The Economist print edition

Scientists are still struggling to understand a new mystery virus

WHAT is it, where did it come from, how is it spread, and can we stop it? These, in a nutshell, are the questions that scientists are still struggling to answer after Severe Acute Respiratory Syndrome (SARS) was first reported in Hong Kong in mid-March.



In the race to identify the cause of the disease, two alternative agents have already been proposed. But Klaus Stohr, a virologist for the World Health Organisation (WHO), says he is confident there is enough evidence to implicate a type called a coronavirus, which belongs to a family of viruses that can cause, among other things, the common cold in humans.

This confidence comes even though too little time has elapsed to satisfy the usual epidemiological requirements (known in the business as Koch's Postulates) for demonstrating that a particular agent causes a given disease. But Mr Stohr says that, of 55 SARS patients tested, 45 either had the virus in their faeces, or had antibodies to it in their body fluids. Moreover, the virus has been isolated from patients during all stages of the disease. That is convincing, if not conclusive, evidence.

It is still not known where the virus first came from but genetic work suggests it is related to mouse hepatitis C, transmissible gastroenteritis in pigs, and the human coronavirus (which is rarely fatal). Such links add weight to the theory that the disease originated in livestock in rural China, where humans and animals live in close contact, and then jumped to humans.

Until this week, epidemiologists believed that the virus was spread by the transmission of droplets, that is, through coughing and sneezing. Mr Stohr says evidence for this was found in the success of control efforts in Hanoi, Singapore and Germany—where no subsequent local transmission occurred. But the latest cases in Hong Kong have caused particular alarm because they do not appear to follow a droplet pattern of infection (see article). So new routes of transmission, via air and water, are being explored. And because hardy coronaviruses can survive outside the human body for three to six hours, another possibility being examined is that contact with an object tainted with droplets (such as a telephone) could lead to infection if the person who touched it were subsequently to touch his eyes, nose or mouth.

Without knowing the precise transmission routes, it is difficult to contain a disease. So the WHO recommends that all but essential travel to Hong Kong and Guangdong should be postponed. Since March 9th nine tourists, from countries such as Switzerland, Britain, France and the United States, have picked up the virus in Asia. Fortunately, after the WHO's March 12th alert, health authorities were primed to isolate these cases, and they seem to have prevented any subsequent spread. The alert, though, came just too late to prevent an outbreak in Canada.

Besides Hong Kong, local transmission remains a problem in Beijing, Guangdong, Shanxi and Taiwan. A WHO spokesman said Hanoi had not seen any new cases in eight days, and the outbreak in Singapore seemed to be under control.

At the moment only time and labour-intensive laboratory testing can determine if someone is carrying the disease. What is needed is the capability for mass testing, in order to answer the many remaining

questions, such as how the virus is emitted, whether infected people who are not displaying symptoms can nevertheless transmit SARS, and for how long patients remain infectious.

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Japan

All eyes on North Korea

Apr 3rd 2003 | TOKYO
From The Economist print edition

A satellite signal about security

Get article background

EPA

We're watching you

“A HOSTILE act,” said North Korea. “Japan will be held wholly responsible for sparking a new arms race in North-East Asia.” Diplomat-speak for “rubbish” was the Japanese response. Yet the two spy satellites that Japan put into orbit on March 28th are meant to make the neighbours take notice. Later this year, Japan will add a second pair of eyes in its effort to keep tabs on North Korea. Not only does the North have missiles that can hit all of Japan, but recently it has taken even more threatening steps, by secretly enriching uranium and, when caught doing that, by restarting a mothballed reactor that produces plutonium—both materials from which nuclear bombs can be made. Japan's government is keen that not just North Korea, but also South Korea, China and Russia, the three other countries apart from America that are trying to resolve the new tensions, understand its concern.

Some fear that North Korea will take the satellite launch as an excuse to test one of its own far-flying missiles. That might provoke louder debate in Japan about imposing economic sanctions on North Korea, but there would be little, militarily, that Japan could do. It relies heavily on America for defence against such threats. It also gets regional intelligence from its chief ally. But after North Korea fired a Taepodong rocket over Japan without warning in 1998, the government decided to build its own satellites to monitor what its prickly neighbour was up to. Now that tensions are increasing again in the region, Japan is also talking more seriously to America about co-operation on missile defences.

A poll in January by Japan's cabinet office, reported in the *Yomiuri* newspaper, showed that 43% of Japanese were worried that their country would be drawn into a war. That is the highest proportion since the government began conducting the poll (which it has done roughly every three years since 1969). In the same poll, 74% of Japanese said that North Korea was their biggest concern, up from 57% in 2000.

The new satellites will do little directly to meet the North Korean threat. Even the third generation of satellites, which the government is planning to deploy in eight years or so, will be able to see with only one-third the resolution of America's existing satellites. And it will still be several months before proper analysis of the pictures sent back by the two launched last week can start. Moreover, says Ken Jimbo, an analyst at the Japan Forum on International Relations, a think-tank, Japan would need three dozen satellites to have reliable coverage around the clock. Even then, Mr Jimbo points out, they would be no substitute for the early-warning satellites that America uses to detect imminent missile launches.

Yet their deployment has a purpose. Besides providing intangible solace to Japan's jittery population, as well as pleasing Mitsubishi Electric and other firms who will be involved in building the birds, the satellites are meant to be seen as another sign that the government is now prepared to take more responsibility for Japan's own security. Japan still cannot defend itself properly without help from America, but it is increasingly no longer content merely to shelter passively under America's security umbrella. In more ways than one, Japan is looking at potential threats with new eyes.

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Elections in Indonesia

Through a maze to democracy

Apr 3rd 2003 | JAKARTA
From The Economist print edition

Parliament's attempts at reform

PREPARATIONS for Indonesia's general election started this week, with officials preparing to compile the voting lists. This is not a moment too soon, even though the election is not due until next year. Some 130m people will be voting in about 450,000 polling stations spread over the 17,000-odd islands of the Indonesian archipelago. Free elections are still a novelty in Indonesia. Suharto, the country's dictator for 32 years, held polls for show. Legislators have drafted laws they hope are both practical and allow for democratic choice. Will they work? The auguries are not good.

The draft laws have a byzantine look, as they seek to cope with the creation of political parties, the conditions under which they fight elections, and how seats are allocated. Giving an example of MPs' inexperience, Imam Prasodjo, an election commissioner, says they did not understand how much trouble they were causing by stipulating that each polling station should cater only to 300 voters at the most.

In an effort to reduce the number of parties contesting the poll from the bewildering 48 that took part in 1999, the year after Mr Suharto's fall, parties that won fewer than 2% of the seats will be barred next time. However, it seems that a party can simply change its name, however slightly—from “Justice” to “Justice and Development”, for example.

The MPs have amended the old system of proportional representation. Next year voters will be able to state their preference for a particular candidate, as well as voting for the party of their choice. But voting for a candidate will be optional and many voters may not bother. Those candidates who do well may still not get enough votes to pass the threshold. Democracy activists fear that many parties will work the system to ensure that their hacks are elected.

Under the old system, some constituencies were absurdly large: one had 82 MPs. But a large constituency at least gives small parties a chance to win a seat or two, as happened in 1999. Parliament has told the election commission to provide some constituencies of three to 12 members. The practical result of smaller constituencies is likely to be that even medium-sized parties will wither at the expense of the two biggest, Golkar and PDI-P. Yet parliament has given the commission no detailed guidance on constituency size. Imam Prasodjo says he and his colleagues have not even discussed the matter.

Cynics say the big parties left the decision in the commission's hands only so that they could influence matters behind the scenes without attracting public fury. That may be unfair. But the proposed law on the next presidential election—to be held only two months after the parliamentary election—definitely involves some jiggery-pokery. According to the draft, only parties that win 20% or more of the vote in the parliamentary election will be allowed to nominate a candidate for the presidential one. Smaller parties could form coalitions to meet the threshold, but would have to do so before the parliamentary election. If they turned out to have miscalculated their support, they would not be able to compete. The danger is that only Golkar and the PDI-P, both secular parties, would be left in the running, excluding all the Islamic parties, a sure-fire recipe for instability.

Were it not for the 20% rule, the presidential election could be held at the same time as the parliamentary one. Since the draft law calls for a run-off if no candidate wins half the vote, yet another election may follow two months later. The entire electoral cycle will take almost a year, once time is thrown in for party registration, nominations, and campaigning. If Indonesians knew what lay ahead, they might slam their doors on the officials who have started compiling the registers.

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Australia

Brown and the Greens

Apr 3rd 2003 | SYDNEY
From The Economist print edition

An emerging group shakes the big parties

Get article background

Green light
Australia's House of Representatives
Election results, % of votes

Party	1998	2001
Labor	40.1	37.8
Liberal	33.9	37.1
National	5.3	5.6
Australian Democrats	5.1	5.4
One Nation	8.4	4.3
Greens	**2.6**	**5.0**
Others	4.6	4.8

Source: Parliament of Australia

BOB BROWN seems an unlikely figure to shake up Australia's politics. He is a doctor, one of Australia's few openly gay members of Parliament, and possessed of a gentle manner that seems out of place in the cut-and-thrust of Australian politics. Yet Dr Brown and the Australian Greens, the party he leads, have emerged from the shadows to shake the established parties, Labor and the conservative Liberals, suggesting that the small party, whose roots lie in environmental battling in Dr Brown's home of Tasmania, could be poised to become the country's third political force, eclipsing the National Party, which is in coalition with the Liberals.

At a state election on March 22nd in New South Wales, the most populous state, the Greens doubled their share of their vote from 4% to 8%. This followed a string of upsets in other state and federal polls. In Tasmania last July, the Greens' vote jumped from 10% to 18%, their highest score ever in any state; in Victoria last November it went from 1% to almost 10%. At the most recent federal election, in late 2001, the Greens' vote doubled to 5%. An opinion poll published on April 1st claimed their national support had almost doubled again to 9%. Most spectacularly, the Greens last October snatched from the Labor Party the federal seat of Cunningham, south of Sydney, in a by-election that lost Labor this previously safe industrial constituency for the first time. The Cunningham victory gave the Greens their first seat in the House of Representatives, the federal lower house. They have two members, one of them Dr Brown, in the Senate, the upper house. The Greens now have a total of 17 seats in Australia's federal and state parliaments.

There is more than just an element of protest in the rise of the Greens. Oddly, it was the demise of One Nation, a small party espousing bigoted nationalism, led by Pauline Hanson, that left the ground open to them. Mrs Hanson's legacy was the dragging of John Howard, the prime minister, and his federal conservative coalition government, further to the right. Mr Howard won the 2001 election on a platform of policies towards asylum-seekers that mirrored Mrs Hanson's, an election that Amanda Lohrey, the author of a recent book on the Greens, describes as “a sideshow alley of surpassing ugliness”.

The failure of the opposition Labor Party to attack Mr Howard's hardline treatment of asylum-seekers lost Labor a lot of votes to the Greens; their only state parliamentarian in South Australia is a Labor defector. The war in Iraq has brought more losses. Labor appeared wishy-washy in its opposition to Mr Howard's commitment of 2,000 Australian troops to the American-led attack; Dr Brown blitzed it unequivocally. Labor has most to fear from the Greens, but they are also taking votes from disaffected conservatives who once supported the Democrats, another small party whose star has now faded.

Dr Brown's statements on Iraq and other national issues such as education and health now command almost as much attention on television news as those of the big-party leaders. It may be too early to declare the Greens the new third force. But Miss Lohrey argues that their current level of support could make them the dominant minor party in the federal election due next year. Dr Brown goes further by suggesting that the party could win eight seats in the 76-seat Senate. That would make the Green Party a force to contend with.

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China

A qualified vote

Apr 3rd 2003 | BEIJING
From The Economist print edition

And better not be rude about the party

IS DEMOCRACY spreading at last to China's cities? After several years of much-trumpeted direct elections of village chiefs, urban areas are now introducing the idea of one person, one vote, secret ballots and independent candidates. But it is a cautious process.

This is not about hustings for mayors. The urban equivalents of village chiefs are lowly neighbourhood committee leaders. The committees help the government maintain order and provide services such as medical advice and recreation facilities. Four years ago a few provinces introduced direct elections for some neighbourhood leaders. Now the practice is more widespread. In the first half of this year, some 10% of the capital's 2,400 or more neighbourhoods are holding direct elections for the first time (others prefer China's time-honoured practice of shooing in Communist Party favourites).

These elections give people a sense of what real elections are and what democracy is, says Li Fan, director of the World and China Institute, a non-governmental think-tank. Mr Li has been helping officials in the eastern city of Ningbo, the first big town to conduct direct elections in every neighbourhood of an entire district (urban Ningbo has six districts with a total population of 2m). These elections began last month and are due to finish in June. In one Ningbo neighbourhood, Mr Li says, candidates have even been campaigning from open-topped vehicles, a practice hitherto hardly to be thought of.

Openly attacking the Communists, let alone forming a rival party, is still out of the question, though. And just like the directly elected village chiefs, committee leaders still have to obey the orders of neighbourhood Communist Party secretaries—though they are often one and the same person.

In Jiudaowan, a part of Beijing, the party secretary won a landslide victory last August when her neighbourhood became the first in the capital to conduct direct elections. But she may find that her three-year term of office is her last in Jiudaowan, a warren of old alleyways and single-storey courtyard homes dating back to the Qing dynasty. Many communities like Jiudaowan's are being uprooted as the ancient city is bulldozed to make way for new development.

One reason why the capital is reluctant to see grassroots democracy spread is that neighbourhoods are often resentful of this upheaval, says Wang Jinzhuo, of Beijing's New Citizen Education and Research Centre, a private institute that helped devise Jiudaowan's elections. Officials fear the emergence of real public opinion would make life difficult for the government, says Mr Wang. So much for democracy.

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Zimbabwe

Wanted: new driver

Apr 3rd 2003 | HARARE
From The Economist print edition

AP

Can Robert Mugabe's regime be ousted peacefully, or will he cling on till his country is wrecked?

Get article background

A DOZEN soldiers, in uniform, came to Renford Mudzi's home after midnight. They held and tortured him for three days, beating his feet, face and buttocks, and running electric shocks through his toes, tongue and penis at such voltage that it sent him into convulsions. They accused him of having burned a bus during Zimbabwe's recent general strike, which he denies. His real crime may have been that he is an activist for the Movement for Democratic Change (MDC), the country's main opposition party.

From his hospital bed, where he is recovering from head injuries and two cracked vertebrae, Mr Mudzi laments that his family has had to hide in four different homes in six weeks. For their sake, he asks that his real name not be published. But he insists that he will never quit the MDC, nor rest until democracy returns to Zimbabwe. His wife, he says, backs him, despite the suffering his stance has brought the family.

In recent weeks, the Zimbabwean opposition has found a new energy, and the government has grown jittery. On March 18th and 19th, an MDC-organised general strike brought most of the country's surviving businesses to a halt. This week, despite spirited rigging by the ruling party, ZANU-PF, the MDC won two parliamentary by-elections. And March 31st marked a deadline that the MDC leader, Morgan Tsvangirai, gave to Mr Mugabe's regime to restore some basic aspects of democracy or “face a popular mass action to regain the people's liberties, freedoms and dignity.”

He has yet to give any details, but Mr Tsvangirai apparently hopes to lead a series of big demonstrations as a “final push” to send Mr Mugabe's regime the way of Nicolae Ceausescu's. In the past, the party has hesitated to take to the streets, for fear that Mr Mugabe would roll armoured cars over the protesters. As a result, the government has been able to pick them off one by one.

Mr Tsvangirai, for example, is currently on trial for alleged treason, with two colleagues. His deputy, Gibson Sibanda, was arrested this week for allegedly breaking Mr Mugabe's security laws by helping to organise the strike. And in the past two weeks, hundreds of MDC supporters have been picked up and tortured, like Mr Mudzi, by special army units, the police, or by Mr Mugabe's youth militia. Harare's

casualty wards groan with the victims, some with broken bones, others with burns. One grandmother told this correspondent how a soldier raped her with the barrel of his rifle. Remarkably, few injured activists show any sign of giving up.

Expecting trouble, the government is taking precautions. Armed police are out in force, throwing up roadblocks and patrolling Harare's streets. Army units guard Mr Mugabe's splendid residence and offices. Shiny new armoured personnel carriers, complete with turret-mounted machineguns, rumble vigilantly around potential trouble-spots.

Against such firepower, the unarmed opposition would seem to stand little chance. Few imagine that Mr Mugabe would hesitate to give the order to open fire. But his footsoldiers' morale is open to question. In private, some police say they are appalled at their masters' systematic use of torture. Some ZANU members of parliament admit that their party has lost popular support.

The main reason is not the government's brutality; it is the desperate state of the economy, which is thought to have contracted by 30% in the past three years. Inflation has hit 220%, and unemployment is perhaps 70%. Worst of all, thanks in large measure to Mr Mugabe's policy of seizing white-owned commercial farms, two-thirds of the country's 12m people are either subsisting on food aid or going hungry. Price controls have caused staples such as maize meal, sugar and cooking oil to vanish from the shops, to the delight of black-marketeers, who are often ruling-party hacks or army officers.

Last month, the Commonwealth announced an extension to Zimbabwe's suspension, imposed after Mr Mugabe stole a presidential election last year, and some western countries have imposed an asset freeze and a travel ban on Mr Mugabe's closest cronies. But with all attention on Iraq, it seems unlikely that outsiders will exert serious pressure on the regime. South Africa, Zimbabwe's most influential neighbour, is actively seeking to end its isolation. So Zimbabweans will have to help themselves. Mr Tsvangirai predicts that they may have to make “extreme sacrifices...even the supreme sacrifice, to get rid of Mugabe.”

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Eritrea v Ethiopia

Oh no, not again

Apr 3rd 2003 | ADDIS ABABA AND ASMARA
From The Economist print edition

Poised on the brink of another pointless conflict

IT LOOKS like an ordinary farming village: stone houses, a school and a few shops, clustered around a dusty main street. Badme is not the sort of place you would kill for, but 70,000 people died in the war Ethiopia and Eritrea fought over this village of 5,000 souls and the nearly-empty plain that surrounds it. And though the conflict officially ended three years ago, there are signs that the two sides may soon start shooting again.

On March 28th, an independent commission, appointed by both countries to determine where their border lies, released a final verdict: that Badme is in Eritrea. This followed a ruling in April last year that ran to 135 pages but failed to indicate clearly whether the village was Ethiopian or Eritrean. The new verdict delighted the Eritreans, but Ethiopia immediately disputed it, despite having previously agreed to treat the commission's judgment as “final and binding”. Senior officials openly talked of a renewal of hostilities; the head of the government of the border region of Tigray declared that “one way or another, there will be skirmishes.”

Meles Zenawi, Ethiopia's prime minister, says he will not give Badme up. To diplomats from aid-giving countries, he argues that his generals will not accept the loss. If Badme goes to Eritrea, his government may fall, he claims, causing chaos. Ethiopia is large and volatile, and its region, the Horn of Africa, has some strategic importance, so foreigners do not dismiss this plea out of hand.

Eritrea is smaller and less crucial, but has international law on its side. Its government has accused Ethiopia of massing its troops along their common border. Ethiopia denies it. The Eritrean president, Issaias Afwerki, has appealed to outsiders to enforce the law.

The UN is caught in the middle. It has 4,200 peacekeepers in the border zone, with an annual budget of $206m. But, despite three years of mediation, little has been resolved. The two sides are still arguing over the same piece of land that sparked the war, and the two leaders appear to hate one another even more than before. Those who know them personally believe that neither will back down. Senior UN officials privately admit that they are “seriously worried” and have run out of ideas.

The demarcation commission could have done a better job. Because its ruling last year ducked the most important symbolic issue of all—Badme—both sides were able to announce that they had been awarded the village. The Ethiopians who live in Badme were allowed to remain, while the Eritreans who had lived there before the war, but fled to avoid the Ethiopian army, fester in temporary camps in Eritrea. It is not yet clear what will now happen to either group.

The UN was hoping to have pegged out the border with markers within 18 months of its arrival, but has not yet started, citing, among other things, fears for the safety of its personnel. Guerrilla activity along the border has increased, despite a UN-monitored 600-mile (965km) buffer zone.

Meanwhile, both countries have used the military threat from the other as an excuse to stifle dissent. Eritrea's first democratic elections, which were to have been held in 2001, have been postponed indefinitely. The independent media have been shut down, and several journalists and politicians suspected of disloyalty have been jailed. The country remains on a war footing, with thousands of young men and women drafted into the army or made to carry out heavy manual labour at the government's pleasure.

In Ethiopia, perhaps 75,000 suspected Eritreans have been rounded up and deported. Last year, in two southern regions, policemen opened fire on crowds and razed entire villages after raucous

demonstrations by local opposition groups. The official death toll was 140, but aid workers reckon 400 died. The press is under siege, too. A proposed new law would allow officials to spike stories they dislike and to imprison journalists who disobey.

Ethiopia remains popular with donors, however, because the government is at least making some efforts to democratise. This enrages Eritrea. Last week, Woldai Futur, one of Mr Afwerki's advisers, accused the West of double standards: “There are people arrested here, put in jail. In Ethiopia, people demonstrated and were massacred. [Yet] the European Union found it important to take a position against Eritrea and reward Ethiopia.”

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Jordan's secret police

Behave, or else

Apr 3rd 2003 | AMMAN
From The Economist print edition

Why Jordanians fear to protest too loudly

Get article background

AT RALLIES in the forecourt of a trade-union building, a 13-year-old girl stirs Jordan's angry white-collar workers with songs of Palestine and Iraq. “O freedom fighters of the world arise,” Mays Chalash peals through loudspeakers. In the crowd, girls take up her cry: “Get out on the streets and revolt,” they yell at their men. But the men remain safely seated, chanting but not revolting.

Two weeks into the war in Iraq, the Jordanian street is surprisingly calm. In the Palestinian shantytowns that hug the capital, Amman, ten-year-olds fling stones at policemen. But few men join in. Why? No doubt, vanloads of riot police lining the roads give would-be protesters pause for thought. But what most deters them is the all-pervasive *mukhabarat*, or secret police.

All Middle Eastern regimes try to strike at least a little fear into their subjects. Jordan's government is the most decent of the bunch, but citizens applying for almost any formal job must submit a reference of good behaviour from the *mukhabarat*. Without it, they—or even their children—may find access to college or promotion barred. In effect, all adults are subject to security vetting.

Rafia, a veteran of the Palestinian *intifada*, is not alone in saying he wishes to volunteer to fight the infidels in Iraq. But he hesitates to bear the consequences of an Iraqi stamp in his passport. “It's not the dying in Iraq, I'm afraid of. It's what happens if I return alive,” he says. Friends, stripped of their security approval after they were rounded up after street protests, are now jobless and passportless, trapped in a kingdom without welfare support.

A few Jordanians benefit, however, from all this snooping. Students at Jordan University's Islamic law faculty can help pay their way through college by filing reports on over-zealous colleagues. Payments come cheap at $6 per file, but the best informants can win scholarships. It's an ill wind.

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West Europe's Muslims and the Iraq war

No war in their name—but no jihad against the West either

Apr 3rd 2003
From The Economist print edition

Reuters

Most Muslims in west European countries are fiercely critical of the war. But not so fiercely, their leaders hope and urge, as to be out of step with other critics

Get article background

“THANK you, Germany,” said one banner as Berlin Muslims last weekend protested against the Iraq war. Like most Muslims in western Europe, they are appalled by it. But there is a hint of a silver lining: so are most Germans, not least Gerhard Schröder, and most west Europeans are against it; and that shared feeling may be bringing together the natives and the Muslim minority.

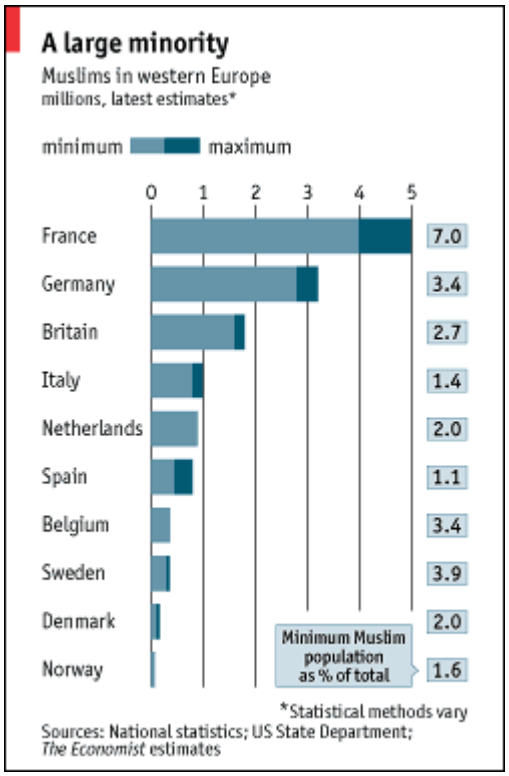
Not only in Germany, and not before time: the two groups have been drifting apart, especially since September 11th. Germany's 3.2m Muslims are mostly Turks. But they have felt, and resented, the suspicion as police raid mosques and other Muslim centres to catch Arab terrorists. In the Netherlands too its 850,000-plus Muslims have felt increasingly suspect; especially the many Moroccans, says Mohamed Sini, one of their leaders. But now, he says, relations are improving again, as the native Dutch—mostly against the war, though the prime minister backs it—see Muslims reacting much as they do.

“Here too,” says Lhaj Thami Breze, president of the Union of Islamic Organisations in France (UOIF): “We are proud of Chirac and France.” All the main French Muslim bodies got together as the war began, to congratulate the government on its outright opposition. In Spain, 90% of voters oppose the government's support for the war. And just as they have seen through its “anti-democratic” lies about the war, claims Mustapha El M'Rabet, president of a Moroccan immigrant body, so too they have begun to realise—he says—that the government has given immigrants an unfairly bad name .

So most Muslims feel just as most other Europeans do? No. They feel it much more strongly. “We're Arabs and Muslims,” says Mr El M'Rabet, “and we see an Arab, Muslim country being attacked.” Muslims also see it more vividly than most Europeans, on satellite television from Turkish or Arab stations or in e-mailed pictures from the al-Jazeera website. So behind the words of Muslim spokesmen it is easy to detect a deep anxiety to keep Muslim protests within democratic bounds, and visibly in tune with those of the host communities.

Specifically Muslim demonstrations have been notably—and deliberately—few. The Berliners cited above were on their own, but they were only a couple of hundred, whereas tens of thousands of Germany's Muslims have taken part in protests by the population at large. Britain's Muslims are as hostile to the war as any others: “A black day in our country's history”, said the Muslim Council of Britain. But they have carefully kept in line with other anti-war groups, especially since the fighting began and most Britons “rallied round the flag”. London has seen one big Muslim march, but it was the work of an extremist body that most British Muslims disavow. Protests like the plan in Denmark to turn the square outside Copenhagen's city hall into a vast Muslim prayer meeting on April 4th have been a rare exception.

Equally, Muslim leaders have urged their followers to show restraint. Demonstrate, boycott American goods, fly peace flags, but no violence, said Italy's Union of Islamic communities; and as for the call for *jihad* that recently came from Cairo's Islamist sages—well, it “must be interpreted”. The mosques of France, while deploring the war, have united in an appeal for calm and dignity in response to it. “We want no provocation or extremism,” says a spokesman for the grand mosque in Paris, and even more fiercely Islamist bodies such as Mr Breze's UOIF echo those words.



What these French Muslims are thinking of is the attack made by some Muslim protesters on some left-wing Jewish ones during a Paris demonstration last month. They know that nothing could discredit Muslims in Europe more than letting their protests earn the label of anti-Semitism. Notably in the Netherlands, Muslims have mostly worked to form a common front with some Jewish and church bodies.

Muslim leaders are likewise eager to damp down views, held by many of their followers, that put Muslims outside the European consensus. They condemn the war: it's an aggression, a breach of international law, a crime against humanity, they say; it's about oil or recolonising Iraq or aiding Israel or George Bush's ego, or whatever. And it is hard to find any Muslims—even if they want Saddam Hussein removed—who think liberating Iraq is really Mr Bush's aim. But support for the Iraqi president, common enough on “the Arab street”, is almost as hard to find among Europe's Muslim leaders.

His is “a cruel regime”, say those of Italy. “A dictator,” says Ayhan Tonca, a Turkish-Dutch leader, and the Moroccan-Dutch Mr Sini says it just as readily. Even the outspoken Mr Breze, in Paris, uses the word, though he adds that, as between attacker and attacked, one must back the victim. Young Muslim protesters are tending to wave pictures of Mr Hussein, at times beside ones of Che Guevara, says Mohammed Bechari, leader of a rival French Muslim body—but so are young non-Muslims.

Still more earnestly do Muslim leaders, however sceptical of American motives, refuse to see this as a war of religion. The idea horrifies them. But they fear that it is spreading, on both sides. Religion “is not Bush's motive,” says Mr El M'Rabet, from Spain, “but he's using it.” Increasingly, says Shahid Malik, a member of the national executive of Britain's Labour Party from strongly Muslim Burnley, in northern England, “Muslims see the ‘war on terrorism' as drifting into a war on Islam.” Listen to both sides' rhetoric, says the director of Islam and Citizenship in The Hague, and the idea becomes ever harder to rebut. And Iraq's resistance, says Abu Laban, a Copenhagen imam, could spiral into a war of Muslims “against the United States, maybe the West in general”. In short, *jihad*.

Inshallah, no. Saddam would love that. It would be bad for the world. For western Europe's Muslims it could be disaster.

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Russia's foreign policy

Which way, really?

Apr 3rd 2003 | MOSCOW
From The Economist print edition

Sidelined by the war on Iraq, Russia could still win the crucial role it seeks

IT HAS been a puzzling couple of weeks for Kremlin-watchers. Until the Iraq war began, many had interpreted the mixed signals from Russia—threats from hardliners like Igor Ivanov, the foreign minister, that Russia would veto any vote in the UN Security Council for war, and soothing assurances from moderates that it would not—as Vladimir Putin's way of letting the differences among the Moscow elite be aired. Surely, once diplomatic channels were exhausted and the assault begun, the ever-pragmatic Mr Putin would shrug and get down to the important business of repairing his friendship with George Bush.

Not so. Since the first strikes, Russia and America have been squaring off like boxers. Mr Putin called the war a “big political mistake”. Mr Bush retorted by airing old complaints that Russian companies had broken UN sanctions on sales of military equipment to Iraq. Russia released documents with similar claims about western firms, complained about American spy-planes flying over neighbouring Georgia, and its parliament put off the ratification of an arms-reduction treaty, while the criticisms—and even calls for a halt to hostilities in Iraq—grew ever more shrill.

Why? Foreign-policy splits in Moscow, as in Washington, are nothing new. For Russia's hawks, snubs and slights by the West rankle—whether it be the humiliation of Russian forces in Kosovo in 1999, the expansion of NATO to include former Soviet satellites, or America's withdrawal from the Anti-Ballistic Missile Treaty last year. In particular, the hawks feel that Mr Putin has conceded too much. Maybe the opportunity to drive a stake into NATO's heart was just too tempting to resist.

Iraq may have been the last straw, forcing the president to take a tough line to appease them. But some think that Mr Putin himself feels frustrated. “He's sincerely concerned that the whole Iraqi debacle will destabilise the region close to Russia's borders,” says Lilia Shevtsova, of the Carnegie Endowment's Moscow think-tank. “And he's using Iraq to demonstrate that he's unhappy with the partnership with Bush, that it's insulting for Russia.”

Mr Putin's trouble is that, however disadvantageous the relationship with America may get, he has little alternative to it. Though the phrase “multipolar world” pops up ever more often in Russia's foreign-policy discourse, its most important strategic and economic ties are with the West. Even its attempts to restore its Middle East relations are floundering again. Having agreed on oil-production quotas with OPEC earlier this year, Russia was furious when the cartel allowed its members to flout them to ensure oil supplies during the war, causing the price of oil, a mainstay of the Russian budget, to fall precipitously.

Above all, ties with the West mean ties with America. For all Mr Putin's frenetic trips to Paris and Berlin before the war and his expressions of solidarity with France and Germany, he is “an American more than a European”, says Sergei Karaganov, a foreign-policy pundit close to the Kremlin. Europe may matter more to Russia in trade terms but, strategically, Messrs Putin and Bush think alike. Both want to slim their nuclear arsenals; both believe they face threats from terrorism and Islamic radicalism (in Russia's case, potentially from its own Muslim population, as much as a fifth of the total, and from secessionists in Chechnya and maybe elsewhere). When Russia's army commits new atrocities in Chechnya or when America goes soft on Israel, it is Europe that criticises while the two former super-enemies turn a blind eye to each others' failings. Even during the toughest moments of pre-war diplomacy, it was the French, rather than the Russians, whom the Americans condemned most.

Moderates in Moscow have been urging Mr Putin to stop playing hard-to-get and patch things up. And for all their harsh exchanges of the past two weeks, Russian and American officials have insisted that they will keep co-operating. “The crisis is not going to let us weaken bilateral relations,” says Alexander Kuznetsov, the foreign ministry's director of planning. On the other hand, Russia, still trying to prevent

the UN (and its role therein) from becoming irrelevant, wants the Iraq issue to return to the Security Council.

On that point, Mr Putin may find an ally in Tony Blair. This, thinks Ms Shevtsova, may be a way for Russia not only to have its own interests in a post-war Iraq considered but also to help the fractured West reunite: “By being a kind of intermediary, joining Blair on certain issues, Putin could gain an invaluable place in the world arena.” That—unlike, say, lining up with France—might help restore the global role that wounded Russian pride demands. But will Mr Putin play his cards this way—and would Mr Bush, offered the chance to restore some western unity, take it?

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Spain's prime minister and its media

Information or manipulation?

Apr 3rd 2003 | MADRID
From The Economist print edition

The government has too much media power, and misuses it

SPAIN'S conservative prime minister, José María Aznar, has firmly backed the war on Iraq. Most Spaniards are against it. So, even before fighting began, were most of the media, even on the right, and they are still more hostile today. That is horrid news, as opinion polls confirm, for a party due to face a general election within a year, now led by a man who plans not to stand again but who has no chosen heir. And Mr Aznar's reaction has made things worse. He treats his critics, these claim, almost as enemies of the nation, and the media as if they should shut up. Some even claim to smell a whiff of Francoism in the air.

That may be overdoing things. Besides, the opposition is certainly able to get its message across. It savaged Mr Aznar in a recent parliamentary debate on his Iraq policy. And he has a point when he complains that the left treats his People's Party almost as if it were an enemy of democracy.

Where they stand

Spain's main media

Newspaper	Owner	Latest circulation, '000s	Position on war	Position on Aznar government in general
El País	Prisa	434	Against	Against
El Mundo	Unidad Editorial	312	Against	Critical, previously pro-government
La Vanguardia	Godó group	198	Against	Against
ABC	Correo group	279	For	For, but with some criticisms
La Razón	Planeta	149	For	For

TV station		Audience share, %	Position on war	Position on Aznar government in general
Telecinco	Mediaset (Silvio Berlusconi)	20.9	Critical	Neutral
RTVE	Public/Government	24.1	For	For
Antena 3	Telefónica	20.1	For	For

Sources: Taylor Nelson Sofres; Oficina de Justificación de la Difusión; *The Economist*

Still, the charge that Mr Aznar misuses the media, particularly television, has some force. Anti-war demos? The main state television channel handled one big demo by showing a 1950s film; the less popular channel wheeled in pundits to underestimate the number of demonstrators. The public is unconvinced of the horrors of Saddam Hussein's arsenal? Replace the scheduled programme with a documentary on the nastiness of chemical warfare. It has been harder to hide the horrors of war itself, but not hard enough to stop liberals demanding an end to the cynical way Spanish governments—this is not the first—use state media as a political tool.

The state is still a big owner and bigger voice in the media. It appoints the heads of state television, radio and the national news agency, EFE, and its message seeps down to their lowest levels. There is little objectivity in the selection of images on state television or in its blending of news with views. When the authorities, central and local, mishandled the oil spewed on to north-western Spain by a sunken oil tanker last autumn, rather than show the filth, state television preferred pictures of the defence minister, Federico Trillo, in his helicopter above pristine beaches. Some employees of the state network last month set up a “committee against news manipulation”—ie, and they said so, in Mr Aznar's interest.

Before he won power in 1996, Mr Aznar promised to reform the law on state media in the direction of objectivity. It has not happened. In his early years of office, Telefónica, the then state-owned telecoms

company, bought up many media outlets, and later brought them on-message. There is little parliamentary scrutiny: an official watchdog on the media, partly peopled by political appointees, is ineffective.

Nor have private channels bitten far into the viewership of state news programmes. The only terrestrial television channel, Telecinco, now out of Mr Aznar's grasp, is in the hands of his friend Silvio Berlusconi, Italy's right-wing prime minister. By Spain's limp standards, it has been tolerably objective, and critical when judgment was called for. Thus one Telecinco sketch parodied the type of experts invited on to state television who explained anti-government demonstrations as manifestations of “the Mediterranean desire to be with other people and the need for an evening stroll”. But after Telecinco recently scrapped a popular political satirical programme, *Caiga quien caiga* (Fall whoever falls), Spaniards wonder how long this relatively happy state of affairs will last.

The press is another matter. The biggest (and deeply serious) news daily, *El Pais*, is broadly pro-Socialist; *El Mundo*, its livelier conservative rival, is against the war and has recently turned against Mr Aznar too. But rather few Spaniards read newspapers, apart from the two big sports dailies—and much of the provincial press anyway depends heavily on EFE reports.

Do not forget the 1980s and 1990s, say conservatives, when Felipe González and his Socialists were in power. In 1986, after he did a U-turn to keep Spain in NATO, the state media were marshalled to crowd out those who were against it. The sycophantic political interview that is so evident on television today was perfected during Mr González's days of power.

Paradoxically, the best days of media freedom came soon after Franco died in 1975, under a conservative government. As Spain headed for democracy, its new prime minister, Adolfo Suárez, had been Franco's director-general of state broadcasting. But the forerunner of Mr Aznar's centre-right People's Party, not wanting to be seen as “old dogs in new collars”, handed control of the state media to the Socialists. It was the left that reverted to Francoist patterns, says Mr Aznar, a charge he made much of in 1996.

Still, there are antidotes: a legion of press columnists, and Spain's free-ranging, private-sector radio, led by such legends as Iñaki Gabilondo and his irreverent morning show on SER, owned by the big Prisa group, owners of *El Pais*. And Mr Aznar could do worse than set the state's media free. If the Socialists win next year's general election, his People's Party will face hostility from the Prisa outlets and the state media too.

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Germany's opposition

Doubly divided

Apr 3rd 2003 | BERLIN
From The Economist print edition

The conservatives are divided, over war in Iraq as well as economics

THE war in Iraq is dividing Germany's conservative opposition. It has traditionally been staunch in the Americans' favour. But Angela Merkel, the Christian Democrats' leader, is coming under fire from within her own party for her outspoken support of the American-led assault on Iraq. In contrast, Edmund Stoiber, the Bavarian premier and the conservatives' candidate for chancellor in last September's general election, is distancing himself from the war—and the Americans.

Life is not easy for the conservatives. For all the widespread disapproval of his government's social and economic policies—his Social Democrats and their trade-union friends were exchanging blows on that this week—on Iraq Germans are massively with Chancellor Gerhard Schröder. Over 80% of them oppose the war, including nearly three-quarters of conservative voters. As many do not believe it will lead to a lasting peace in the Middle East.

Anti-war feeling is particularly strong in Catholic-dominated Bavaria, where Mr Stoiber's Christian Social Union (CSU), the Christian Democrats' sister party, faces a state election next autumn. During the general-election campaign, Mr Stoiber spoke out forcefully against any attempt by the Americans to “go it alone” in Iraq, even suggesting that they should be denied the right to fly over German territory if they did. A few months ago, however, he sought to get more in synch with Mrs Merkel by calling on Germany to “stand by America's side, even in a military conflict”.

But more recently he has swung the other way again. Since the Americans invaded Iraq without winning a further mandate in the UN Security Council, he has sounded increasingly critical. The CSU is “upset” by a war it “did not want”, he says. “The allies will never be in a position to turn the military process into a political and economic success.” And though everything should be done to avert further damage to the transatlantic partnership, “not everything has to be approved of”.

Mrs Merkel, on the other hand, has become increasingly bold in backing the Americans. Even before war broke out, she had endorsed the final American ultimatum to Saddam Hussein. “War”, she said, “had become unavoidable. Not acting would have caused more damage.” It was out of the question, she said, for the Christian Democrats to remain neutral. They must “stand by America's side”, though she declines to say whether, had she been chancellor, she would have committed German troops to the battlefield.

Many of her colleagues think she has already gone too far. Peter Müller, the Christian Democratic premier of the Saarland, who is a former constitutional-court judge, says the war is illegal. Wolfgang Schäuble, who speaks for the party on foreign policy, has called it a “big risk”. His predecessor, Karl Lamers, calls the American claim that Iraq posed a direct threat to the United States “nonsense”. The party's rank and file is perturbed. Many have resigned in protest.

Mrs Merkel knows she is taking a gamble. For the first time in six months, she has fallen behind Mr Schröder in the opinion polls. Her party, while still 13-17 points ahead of the ruling Social Democrats, is also losing ground. Many conservatives are worried. They remember the start of the 1970s when, against the wishes of the great majority of Germans, the Christian Democrats opposed Chancellor Willy Brandt's *Ostpolitik*—the policy of seeking a dialogue with communist regimes (especially the German one) to the east—and found themselves out of power for over a decade. That, they fear, could happen again. But, as a former East German, Mrs Merkel believes strongly in the transatlantic link and thinks her strategy will pay dividends in the long run. Among those who back her, some point out that letting the Americans put their missiles on German soil in the 1980s was unpopular too—but was vindicated over time.

The conservatives' internal rows over Iraq have been exacerbated by Mr Stoiber's decision to present his

own radical plans for reforming Germany's labour market and welfare system, in response to those presented by Mr Schröder last month. The Christian Democrats, who were not even consulted beforehand, were furious, seeing Mr Stoiber's move as a ploy to make up some of the ground he had lost to Mrs Merkel after his defeat in the general election. The Bavarian leader clearly hopes to lead the conservatives for a second time into battle in the next general election, due in 2006. But Mrs Merkel, who is 14 years his junior, is determined not to bow to his wishes again.

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The European Union

Going military

Apr 3rd 2003
From The Economist print edition

Is the EU's modest force in Macedonia a harbinger of bigger things to come?

AP

New badge, new army?

THE European Union has turned into a military power—of a sort. On March 31st the EU launched its first military mission, when it took over from a NATO-led peacekeeping force in Macedonia. Javier Solana, the EU's foreign-policy chief, and George Robertson, NATO's secretary-general, were both on hand to welcome this "new era for European security".

The political symbolism of the Macedonian mission is more compelling than its military clout. There will be 320-plus troops on peacekeeping duty, based in Skopje, the Macedonian capital, with—initially—a German admiral in overall command and a French general in operational control. But from the EU's point of view the important thing is less what the soldiers are doing or who commands them than the fact that they will be wearing the Union's badge, 12 yellow stars on a blue background, on their uniforms.

For years, the EU has had to put up with jibes that it is an "economic giant and a political dwarf". For a decade, however, it has been trying to develop a common foreign and security policy. In recent years this has concentrated on efforts to develop some sort of military muscle. EU leaders have pledged to develop a 60,000-strong rapid-reaction force, which would draw upon the armies of EU countries. Senior military men have been seconded to the EU and have been twiddling their thumbs in their very own "situation room". Now, at last, they have a situation to deal with.

An uprising by ethnic-Albanian rebels in Macedonia linked to militias based across the border in Kosovo, also populated by ethnic Albanians, brought Macedonia close to civil war in 2001. A peace deal was negotiated by EU diplomats, with NATO providing peacekeepers to patrol "crisis areas". One of the attractions for the EU of taking over now is that the situation seems quiet and under control, so offering an uncontroversial début for its new military arm. The hope is that if things go well in Macedonia, the EU will be able to take over the much larger NATO-led peacekeeping mission in Bosnia, where 12,000 troops are on duty.

There is cause, however, for scepticism about the EU's assumption that the Macedonian problem is really under control. The country is still subject to a seemingly endless cycle of private vendettas and politically-related killings, and plagued by smuggling rings and rebel armies, many of whose members are dedicated to the rise of a Greater Albania.

NATO's force in Macedonia has, in fact, done little to tackle these problems. Its troops have specialised in symbolic patrols, with much waving at children and throwing them sweets. The EU is expected to adopt a similar *modus operandi*. Its autonomy from NATO is, in any event, fairly limited. The EU force is using NATO plans and equipment—and NATO promises to take over again, if things get nasty.

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Charlemagne

All aboard the Euro-train!

Apr 3rd 2003
From The Economist print edition

The European Union's expansion is roaring ahead, with destination unknown

OPERATION EU enlargement is going well. The European Union's advance into central Europe is meeting little opposition; the natives are greeting the invading army of Eurocrats with flowers and celebration. Ten countries are holding referendums this year on joining the Union. Two tiddlers, Slovenia and Malta, have already voted in favour by unexpectedly big margins. On April 12th Hungary is likely to plump eagerly for membership.

Recently Günter Verheugen, the EU commissioner for enlargement and chief overseer of the Union's expansion, got a huge ovation from an audience of students at Budapest's University of Technology, one of the main sites of Hungary's ill-fated uprising against Soviet rule in 1956. Mr Verheugen deserved his moment of triumph. Getting the EU's 15 current members and the ten incomers to stick to the commission's "road map" for enlargement was a tricky business—a bit like herding cats. Once minister for Europe in a German government, Mr Verheugen needed all his skills and tenacity to enforce compromise and bring a hugely complicated project to completion.

Yet his triumph is tinged with irony. Mr Verheugen is a passionate advocate of enlargement. But he is equally passionate in his belief that Europe needs "political union", involving much deeper integration in the making of foreign, defence and budgetary policy. Many believe these two passions are fundamentally at odds with each other and that a larger EU will simply be too diverse and unwieldy for a real political union. "Nonsense," retorts the man himself. He has long argued that an enlarged Union would pave the way for political union rather than block it. The new members, he insists, are not the prickly, sovereignty-minded nationalists sometimes portrayed; on the contrary, argues Mr Verheugen, they are keener on political union than are many current members.

But he is dodging an awkward distinction between a political union's form and its content. "New Europe", to use the incendiary phrase of Donald Rumsfeld, America's defence secretary, may be ready to accept the idea that the EU should adopt a common foreign policy by majority vote, something Mr Verheugen deems essential to political union. But, as the Iraq crisis has shown, it is far from clear that the so-called new Europeans would vote for the kind of foreign policy that Franco-German advocates of political union have in mind. Mr Verheugen, for example, believes his native Germany has reached a turning-point. Hitherto, he says, Germany has always striven to be equally committed both to the EU and to the transatlantic alliance. Now, he says with obvious approval, Germany may be ready to accept France's vision of a Europe that acts as a "strong partner but also a counterweight to the United States". The central Europeans, however, are far from ready to make this leap. Indeed, the Hungarians, Poles and Czechs recently outraged France's President Jacques Chirac by signing a letter of support for American policy on Iraq. The Hungarians have let the Americans train Iraqi exiles on their soil (though this week, the training camps were mysteriously closed). The Poles are even contributing troops to the war.

For all his insistence that the EU's expansion will help the cause of political union, Mr Verheugen seems to be preparing a fall-back position. In January he and Pascal Lamy, a French colleague at the commission, proposed that France and Germany should form a "Franco-German union", involving the merger of their armies and diplomatic services, joint cabinet meetings and the adoption of common positions in all EU and international negotiations. Alternatively, says Mr Verheugen, a larger group of the countries keenest on integration could be an "avant-garde" within the EU. He is enthusiastic about a summit between Belgium, France, Germany and Luxembourg (and maybe some others) later this month, aimed at promoting the idea of a European army. It is no coincidence that this is the same quartet which led the opposition within NATO to America's drive to take on Saddam Hussein.

Such a development unsettles the "new Europeans" whose cause Mr Verheugen has championed. In the

recent dispute within NATO, the Hungarians, Poles and others lined up alongside the Americans, not the French and Germans. More generally, the central Europeans have always insisted they will not settle for “second-class”EU membership. The formation of an integrationist “club within a club”, just as the new members join the Union, would look like the creation of just such second-class status. Mr Verheugen tries to meet these objections by insisting that his proposed avant-garde would not be meant to exclude anyone. He says, slightly half-heartedly, that he can imagine the Hungarians and Czechs opting to join an inner core.

The chat-a-Magyar choo choo

The difficulty of the drive towards political union does not, of course, make it downright impossible. Membership of the EU does seem to draw countries together: endless discussion of fish quotas and health-and-safety rules seems to be a bonding experience. Most EU countries, even in central Europe, share elements of France's concern about the use and abuse of American power. But whereas Mr Verheugen's expansion of the EU was due largely to a very precise legal and diplomatic road map, there is no such master plan for political union.

For now, however, such concerns are still tucked away. In central Europe, the next few months may witness an impressive string of votes in favour of “joining Europe”. Mr Verheugen's pre-referendum trip to Hungary culminated in one of those pieces of political kitsch beloved by the EU: a scenic train-ride on the old Orient Express, with the commissioner mingling merrily with assorted pensioners and trade-unionists, then posing for photographers at the locomotive's controls. The European train is indeed rolling forward. New passengers are jumping eagerly on board. Only the final destination has yet to be determined.

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The economy

Brown at the edges

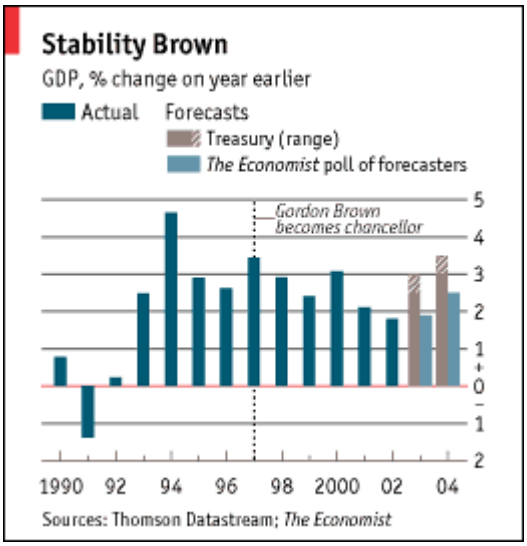
Apr 3rd 2003
From The Economist print edition

The chancellor has delivered stability but is now under-playing the risks to growth

BEFORE Labour regained power in 1997, Gordon Brown made two solemn pledges. There would be no return to “tax-and-spend” and there would be an end to “boom-and-bust”. The chancellor has broken the first of these promises. Households and businesses are being hit this financial year by an £8 billion ($12.5 billion) hike in national-insurance contributions. That makes it all the more vital for Mr Brown to honour his other commitment, about “boom-and-bust”. It was the combination of big tax rises with an economic bust and a collapse in the housing market that helped to destroy the Conservative government in the 1990s.

Businessmen and consumers alike have the jitters because of the war, but the economic effect of these is likely to be short. The economy has shown a remarkable stability over the past six years despite two big shocks to confidence. It kept growing when Russia's debt default in August 1998 raised fears of a big downturn. Even more impressively, it has chuntered on through the global slowdown of the last two years.

For once, Britain has proved more resilient to setbacks than other countries. In 2001 the economy grew by 2.1%, the fastest in the G7 group of advanced countries, and only a little lower than its historic growth rate of about 2.5% a year. Last year it grew by 1.8%, the third fastest among the G7.



It would be silly to praise Mr Brown alone for this. But it would be just as silly not to give credit where it is due. His bold decision to make the Bank of England independent has helped keep both inflation at bay and growth at an even tempo. The government's fiscal policy has supported demand in a downturn, whereas countries like Portugal and Germany have had to tighten policy to meet the boa constrictor rules of the euro area's misnamed Stability and Growth Pact.

But Mr Brown is now too optimistic about the outlook for growth. In his most recent economic forecast, in November, he said that the economy would pick up speed again after two years of below-trend growth, with 2.5-3% this year and 3-3.5% in 2004. In next week's budget, he will have to

lower these forecasts to retain credibility. *The Economist*'s panel of economic forecasters is expecting the economy to grow by 1.9% in 2003 and by 2.5% in 2004.

One reason is that the world economic recovery has recently faltered. The setback has been especially severe in the euro area, which accounts for around half Britain's trade. Another problem is fading hopes of a big recovery in business investment after its sharp fall of 8% last year. Thirdly, Britain's long-running consumer boom is due to run out of steam as households scrimp to meet the delayed tax rises announced by Mr Brown last year.

The chancellor could live with a failure to meet an optimistic growth forecast. He will be more hard-pressed if the economy hits real trouble. The risk lies, literally, on the home front. Along with the big boost to government spending, which increased last year at its fastest rate since 1975, the housing-market boom has been crucial in sustaining the economy. Property prices rose by about 25% in 2002 alone. Households have extracted some of this extra wealth by borrowing more in mortgages than they invested in housing.This in turn has bolstered consumer spending, which rose last year by almost 4% in real terms.

Mr Brown's nightmare is that a collapse in house prices removes this prop to consumer spending. The housing market is weakening in London, but has remained more robust in the rest of the country. According to an index compiled by the Halifax, the country's largest mortgage lender, national house prices rose by 1.1% in March and were 23.4% higher than a year ago.

But even if the whole housing market does come down with a jolt, this is unlikely to prove the catastrophe it was at the end of the 1980s. Then, interest rates rose steeply in order to slow down the economy, which had over-heated, causing a resurgence in inflation. Because the economic fundamentals are much sounder today, it seems unlikely that a housing-market bust can singlehandedly bring down the economy. Inflation is under control and employment remains high. If necessary, interest rates can fall still further, for even their current 48-year low of 3.75% is much higher than rates in America, say.

But longer-term prospects too are bleaker than Mr Brown had hoped. Last year, he raised his estimate of potential annual growth in the coming years to 2.75%. This looked unrealistic at the time and looks even more so following the sharp fall in business investment. Businessmen are now complaining that taxation and regulations are hurting the economy more and more (see article).

Slower than expected growth will mean that big budget deficits will persist. With low levels of public debt, the chancellor can easily afford to borrow, but he cannot rely on an economic bounce-back to cut the deficits. That makes another tax-raising budget only a matter of time. Mr Brown was feted for his last one, but he will get a dusty reception when he comes back for more.

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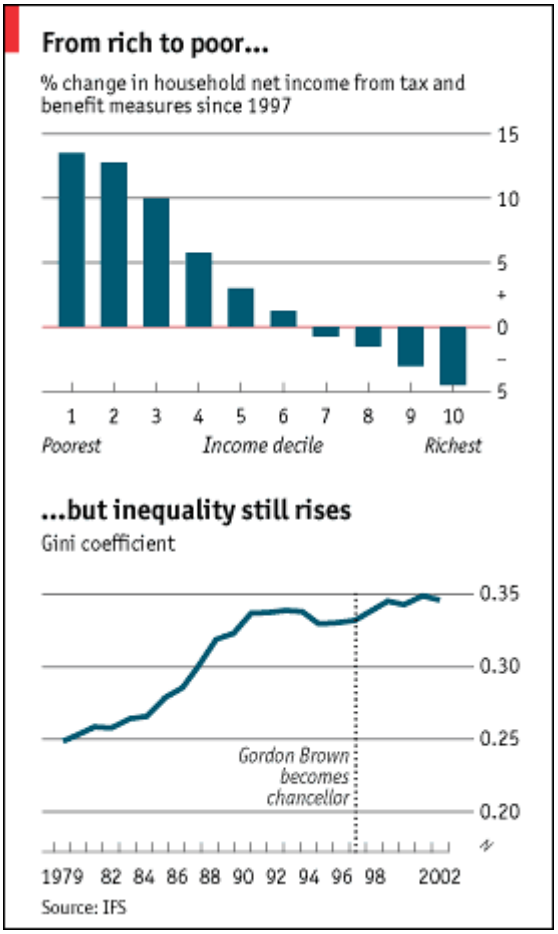
Redistribution

Gordon Hood

Apr 3rd 2003
From The Economist print edition

The chancellor's attempts to emulate Robin Hood are not working

GORDON BROWN has been a highly redistributive chancellor. Income inequality has increased. Which statement is true? No need to ask the audience or to count the coughs: both are.



The Institute for Fiscal Studies (IFS) has totted up the effects of Mr Brown's six budgets since 1997, including measures that come into effect in the financial year starting this week. Its calculations showed that the chancellor has indeed been playing Robin Hood (see chart). A lone parent, for example, is on average £24 ($38) a week better off in today's money as a result of Mr Brown—an 11% gain. Yet overall inequality has risen. A summary measure of the distribution of income is the “Gini coefficient”: the higher it is, in a range from 0 to 1, the more unequal income is. It has increased since Labour took office.

Mr Brown has been rowing against a powerful incoming tide. In order to isolate the effect of his measures, the IFS applied his schedules for taxes and benefits—which it assumed are fully claimed—to the latest estimates for underlying income. It then compared the net income of households with their position if Mr Brown had never been chancellor and the taxes and benefits laid down in the last Conservative budget in 1996, uprated with inflation, were still in place.

The chancellor's problem is that the underlying income distribution has not remained frozen. Since 1996-97, for example, there has been a surge in the number of high-earners. According to the Inland Revenue,

the number of people paying the top rate of income tax rose from 2.1m in 1996-97 to 3.1m in 2002-03. Furthermore, not everyone claims Mr Brown's new benefits, partly because his enthusiasm for means-testing makes them so complicated. The latest official estimates show that up to £4.5 billion worth of means-tested benefits are going unclaimed.

The chancellor prefers to avoid talking about egalitarianism directly, using phrases about reducing child and pensioner poverty. For example, the government has set a target to cut child poverty from 4.2m in 1998-99 to at least 3.1m in 2004-05. But this, too, is proving an uphill struggle. Figures released last month showed that there were still 3.8m children in poverty in 2001-02, only 100,000 fewer than the year before.

Progress has been slow mainly because Mr Brown wants to cut relative, rather than absolute, poverty. His aim is to reduce the number of children living in households whose incomes are below 60% of median income—the level that divides the population, when ranked by income, into two. Households on median income will generally have at least one person in work, whereas many poor children live in households where no one works. So the government has been chasing a moving target as earnings have grown and more families have become two-earner households.

Mr Brown may find it easier to reduce inequality and to cut child poverty from now on. The travails of the City and the bursting of the dotcom bubble mean there are fewer high-rollers than before. Employment is likely to stagnate rather than to rise as it did in the late 1990s.

But these are distinctly mixed blessings, since tax revenue will be less buoyant as a result. Whatever his aspirations to combat poverty, he would surely prefer to have the Treasury's coffers clinking than bare. Redistribution may sound like a lovely bit of fair-mindedness, but the only sure way to get there is through more poverty, not more wealth.

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Business and government

Love Labour lost

Apr 3rd 2003
From The Economist print edition

British business wants a respite from ever-higher taxes and regulation

“IF I were a small firm getting stuck with this stuff, I think I would sell the business,” says Ruth Lea, the head of policy at the Institute of Directors, a lobby group. The “stuff” is reams of regulations and new taxes. In the run up to next week's budget, business lobbies have been waging an increasingly vocal and desperate campaign to get the government to stop what they see as infernal meddling.

When Labour first came to power, tycoons queued up to serve on committees of the great and the good. There was even a sprinkling in the government. Now there are a couple of business people in government at most, and a few assorted media and consulting types hanging around Downing Street. Labour is losing the battle for the hearts and minds of British business.

To be fair, businesses have been mostly happy with macro-economic policy. Interest rates have been fairly stable (which helps planning) and low (which makes borrowing cheaper). And despite the alarming number of shocks to the world economy, Britain's has continued to grow as Gordon Brown, the chancellor of the exchequer, repeatedly points out. He was at it again at this week's British Chambers of Commerce (BCC) conference, though what most delegates would have preferred was some response to their many gripes.

On one big issue—tax—business has been particularly unhappy. This has been going up and continues to do so. In a BCC survey, one in five companies said that they would cut staff as a result of higher national insurance contributions. Together with more parental employment rights and a higher minimum wage, says Digby Jones, the boss of the Confederation of British Industry, another trade lobby, that will add a further £5 billion ($7.8 billion) of costs to British business this year.

But business reserves most of its bile for what it perceives as incessant fiddling and excessive regulation. Not all of this, it is true, stems from the British government; about 40% comes from European legislation. The source is irrelevant to business people—though they suspect the government of being far keener than other European countries on quick and thorough implementation—they just want a stop.

Mr Brown prefers to talk of the myriad “initiatives” that he has brought in to help. His speech to the BCC showed no recognition that the regulatory burden was a problem. But regulation costs money: extra rules introduced in just the past 12 months, says the BCC, have increased costs by £6 billion a year. What is not in doubt is that the owner-managers who form the core membership of the BCC cannot understand, let alone implement, the new paperwork without specialist help.

The raft of family-friendly proposals introduced on April 6th are a good example. “The DTI very sweetly sent us the package,” says Ms Lea, the merest hint of sarcasm in her voice. It is 300 pages. All the measures are seemingly admirable: who could complain, for example, at the right to flexible working arrangements for those with young or disabled children? In a series of advertisements, the Department of Trade and Industry claims: “Employers get a happier, more loyal and more motivated workforce”. But taken together the package is hugely expensive, especially for smaller firms, for whom such flexible arrangements often mean finding someone else to fill in. The government, argue some, is venturing into areas where it has no business to tread, particularly as British companies are already pretty flexible—some 40% of British working women have part-time jobs, compared with 28% for the whole EU.

The more general complaint is that the government is quick to go for blunt regulatory fixes, when sometimes there are other alternatives: education, say, or (whisper it) nothing at all. City grandees worry that the Financial Services Authority, for example, is altogether too draconian, too prescriptive and too rules-bound, particularly with big investors who should be able to look after themselves.

But most businessmen think that they are fighting a rearguard action; few expect the government to change its spots. If the economy stumbles further, an already wary relationship could sour nastily.

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Labour Party

War of attrition

Apr 3rd 2003
From The Economist print edition

Labour's discontents grow as the war against Iraq proceeds

TONY BLAIR has every reason to fear the politics of war. In his very first outing as a Labour candidate, in the 1982 Beaconsfield by-election, he came a poor third and lost his deposit as opinion swung behind Margaret Thatcher's government during the Falklands war.

Two decades later, the stakes are much higher. The longer the war against Iraq goes on, the greater the strain on the party. Last month a group of worried Labour MPs met to discuss what they termed a "haemorrhage" in membership. In recent weeks Labour has lost supposedly safe council seats in Basingstoke, Camden and Abertillery, continuing a trend of losses over the past year.

The omens for the local elections in May are poor. Labour could lose as many as 500 seats. "Most branches are moribund—this is a party dying at the grassroots," claims Mark Seddon, editor of the left-wing newspaper *Tribune*. Some hyperbole from left-wing, anti-war activists is only natural. But in Norwich, a moderate Labour stronghold since 1997, when the party won both the city's parliamentary seats, the mood is downbeat too.

The local Labour Party headquarters has had to put up grilles after a brick was tossed through its window. Ian Gibson, MP for Norwich North, says that a lot of his members are leaving. The party's general committee used to attract 100 members; it is now down to 30. "What happened to the dream?" he says. Steve Morphew, the Labour leader on the council, says it is difficult to enthuse members when "we are carpet-bombing Iraq."

Making sense of the figures nationally is not straightforward. Labour's general secretary, David Triesman, says that, for all the hullabaloo, new recruits outnumber those who have resigned. But few disgruntled members formally resign; most simply let their membership lapse. Party officials admit that overall membership figures are down. The current official total of around 260,000 is near the all-time low reached in the late 1980s, and around a third less than the only recent revival, the 1997 election victory.

The Labour Party has always had a pacifist element but the opposition to the attack on Iraq goes much wider. After the 1991 Gulf war, when Labour was in opposition though in support of the government's pro-war stance, it lost several thousand members. The biggest parliamentary rebellion in modern political history last month, when 139 Labour MPs voted for an anti-war amendment to the government's Iraq policy, will probably accelerate things. Paul Whiteley of the University of Essex, who specialises in the internal workings of the party, predicts that the Labour Party is bound to take "a big hit", much larger than it suffered in 1992.

Nonetheless, the left-wingers' idea that Labour will be left politically and financially ruined by the war is far-fetched. This week David Sainsbury, the government minister and former supermarket chairman, bailed out the party yet again, this time with a £2.5m ($3.9m) donation. But internal dissent puts it in a weak position to fight elections, especially at a local level, where activists' time spent stuffing envelopes, canvassing and talking to people on the doorstep matters more than the line spun by headquarters.

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Transport

Shush, Darling

Apr 3rd 2003
From The Economist print edition

Queue or pay: that is the stark choice for Britain's road-users

TRANSPORT is in such a terrible mess that everyone in Whitehall from the top downwards accepts that the best policy is to say as little as possible—to "park" it, in New Labour parlance. Press releases from the transport department have slowed to a trickle; the minister in charge, Alistair Darling, has adopted a code of silence worthy of a Trappist; but keeping the woes of Britain's sclerotic road and rail networks out of the headlines is proving impossible.

The government's failure to tackle clogged roads has incurred the wrath of the Parliamentary select committee on transport. A report to be published on April 3rd says that congestion by 2010 is certain to be "significantly greater" than it is today. Accusing ministers of manipulating figures, it points out that increases in congestion are now being presented as reductions only because they are less than what might have happened otherwise.

The committee is equally critical of the current emphasis on new road construction, saying it is "astounded" by strategies that work in opposition to Britain's climate-change commitments. Congestion, it says, cannot be tackled simply by building more and more roads. The government must either introduce area-wide road charging or else accept that congestion will continue to rise.

This blunt conclusion is supported by the government-funded Commission for Integrated Transport. In a report to be published next month on the progress of the government's ten-year transport plan, the commission will criticise ministers for failing to get to grips with traffic. Its report is expected to compare London's progress in introducing congestion-charging and improving bus usage with the failure nationally to address congestion on urban roads and motorways.

All this is good news for London's mayor, Ken Livingstone, whose experimental congestion charge has proved a notable if limited success. But it will not go down well with ministers. Already there are whispers in Whitehall that the commission has served its time and that its £1.5m annual budget could be more usefully spent elsewhere.

Shooting the messenger will, however, achieve nothing. The government has itself acknowledged that overall congestion delays will increase by up to 20% by 2010 compared with its original forecast of a reduction of 6%. Mr Darling's position until now has been that area-wide road-charging using satellites is at least a decade away. But he may now have to change his mind. Public acceptance of London's £5-a-day charge shows that the political risks of road-pricing have been exaggerated. The alternative of letting things get ever worse looks less and less sensible. As the transport select committee points out: "A future of increased congestion, pollution and unreliability is not an attractive one."

Mr Darling is shortly to begin a review of the ten-year transport plan, which will be published next year before the 2004 spending review. The Treasury may insist on a faster time-scale for a national road-pricing scheme to offset the huge sums needed by Britain's ailing road and rail networks. A consultation paper to be published later this year on pricing both urban roads and motorways is being considered in Whitehall. The 11 MPs on the transport select committee admit that the radical measures needed to tackle traffic growth may seem politically unacceptable. But as London has shown over the past six weeks, the boundaries of what is possible may be much wider than most politicians appreciate.

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Security industry

Clamping down

Apr 3rd 2003
From The Economist print edition

The government is regulating the private security industry. About time too

PARKING fines are one thing. Extortion is another. Public fury at cowboy wheelclampers, who can immobilise your car on some dodgy or outright spurious pretext, and then demand a hundred pounds or so to release it, has made them among the first targets for a crackdown on the security industry.

In theory, car parks that clamp their customers arbitrarily should go bust. In practice, consumers are in a weak position. One recent scam in a London car park with an exit barrier was an added (and quite illogical) requirement that the ticket must also be left visibly in the car. Drivers who failed to read the small print returned to find their cars clamped.

Instead of some pleasing title such as Ofclamp, the newly established body licensing clamping firms is boringly called the Security Industry Authority. That reflects its wider remit. The other initiative launched this week is intended to raise standards for security guards, including nightclub bouncers.

Almost as unpopular as the wheelclampers, these hulking figures must now pass a criminal background check, an English test and other “training”.

It is true that doormen in some places, such as parts of south London, are little more than a protection racket. And there are enough cases of bouncers selling drugs, or beating stroppy or befuddled punters to death, to create cause for concern.

But there is a danger of over-regulation here. Not all security guards deal with the public. Largely, businesses should be left to choose whom they hire. After all, nightclubs, much more than car parks, live by their reputations.

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Museums

Exhibitionists

Apr 3rd 2003 | GATESHEAD
From The Economist print edition

Opening a glitzy museum is no guarantee of fame and fortune

Get article background

GATESHEAD, said Tessa Jowell, the culture minister, earlier this year, “is the new Bilbao”. A concert and music education centre in glass bubbles designed by Lord Foster is due to open there this year, just up the river from Gateshead's Baltic contemporary art gallery. An award-winning footbridge connects them to the smart Newcastle quayside opposite. The Tynesiders were chuffed. Unfortunately, Ms Jowell has also said the same of Birmingham, Manchester, Liverpool and even Deptford in east London.

The story of Bilbao, once a mouldering industrial port in Spain's Basque country, is popular with politicians because it suggests that investing in art (pleasing one lot of voters) can revive a city economically (pleasing others). Opened in 1997, the Guggenheim Foundation's art gallery, designed by Frank Gehry, boasted 5.2m visitors by 2002. A report by KPMG, a consultancy, reckoned that the visitors spent *euro*776m (£535m) in the region in that period, securing 4,100 jobs and generating *euro*118m in tax revenues, more than repaying the subsidies involved.

If spending on culture really does lead to economic regeneration, Britain should be cashing in by now. The National Lottery and other bodies have spent £4 billion on two dozen or so new art galleries, museums, and science and environment centres, plus smartening up and expanding many existing galleries. This cultural spending spree has brought people to places they would not have otherwise visited. But hopes of economic regeneration as a result may be over-optimistic.

New museums everywhere tend to do well at the start, but then interest tails off. The Guggenheim's turnstiles are slowing down, from 1.3m visitors in 1998 to 851,000 in 2002. Big British successes such as the Tate Modern gallery, which drew 5.3m people in the year after it opened in May 2000 (well above the 2m-3m forecast) may be recycling existing gallery-goers. In the same period, visitors to the old Tate gallery dropped from about 2m to 1.1m.

British regional museum and gallery chiefs asked the government for an extra £50m last year but gained only £23m. As visitor numbers fall, their budgets will come under ever greater pressure. There is a strong case for some state subsidy to art and fancy municipal architecture, but politicians should not kid themselves that this alone can make moribund cities thrive.

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Rural hassles

Country greens

Apr 3rd 2003 | NEWPORT, PEMBROKESHIRE
From The Economist print edition

Officialdom finds environmentally minded country-dwellers an untidy nuisance

A VAST metal farm building glints in the watery spring sun, looking industrial and intrusive in the protected national park landscape. “You can see that from miles around,” says Tony Wrench scornfully. His own home is barely visible, being built out of wood, mud and turf with solar-generated electricity and a compost lavatory. Mr Wrench speaks proudly of its “negligible” environmental impact. Yet it is his building, not the neighbouring agribusiness monstrosity, that the local planners want demolished.

Mr Wrench and his good-lifer chums follow a demanding organic farming doctrine called permaculture, which says that land use should mimic natural ecosystems. Waste and by-products from one activity are used to sustain another. Much the same applies to housing: you build with whatever is available locally, using solar panels or a windmill for electricity.

This sort of eco-heaven is increasingly fashionable. *Permaculture*, a newsletter for just 600 enthusiasts ten years ago, is now a magazine selling 15,000 copies a quarter. Chapter 7, an organisation which advises people how to build low-impact homes like Mr Wrench's, says it helps 600-800 people a year. Lucy Nichol, a planning lecturer at Oxford Brookes University, reckons there are hundreds already living this way, half of them in secret because such homes are illegal under planning laws drafted in the 1950s to stop the countryside being overrun by urbanites wanting a country bungalow. The law, though it is much flouted by the rich or well-connected, says that new houses outside existing settlements must be needed because a worker has to live on the land, say, to look after sheep. The work must also generate enough income, generally £10,000-15,000 a year, to pay a notional rent.

Most permaculturalists and low-impact dwellers do not qualify. They eke out a living from vegetable-growing, craft-making and tending a few animals. A further disadvantage in the authorities' eyes is that permaculture is usually immensely untidy. Low-impact homes, however high-mindedly constructed, often look like messy hovels surrounded by junk that may or may not be recycled one day.

Planners' tidy-mindedness goes against the lip-service paid by officialdom to green living habits. The Pembrokeshire coast national park authority says it “works with local communities towards a sustainable future.” The Welsh Assembly wants “sustainable development” to be the hallmark of the new Wales. The government is thinking of changing the law to allow such low-impact developments. A report published on March 31st by the Countryside Council for Wales argued that they would help reverse rural decline.

But this looks to be too late for Mr Wrench. He hoped nobody would notice his house but it was spotted by planners during an aerial survey (its solar panels were glinting). The local authority has won two appeals and says it will now “take appropriate enforcement action”.

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Bagehot

Mr Blair is not Mrs Thatcher

Apr 3rd 2003
From The Economist print edition

Anti-Europeans have high hopes of Tony Blair. They're in for disappointment

THERE was no great fanfare. Most British newspapers, their thoughts elsewhere, failed even to note the event. But this week, NATO handed over peacekeeping duties in the battle-scarred former Yugoslav republic of Macedonia to a force of 350 soldiers from the European Union (EU). Small beer compared with what's going on in Iraq, but the first time that troops have operated under the EU's flag. Next year, the EU, with Britain and France in the van, is due to take on the much bigger job being carried out by the 12,000-strong NATO stabilisation force in Bosnia.

Peacekeeping is not war-fighting and NATO is still providing much of the back-up. But it does illustrate a couple of things. The first is that, despite everything that has happened in the last three months, it is too soon to declare the attempts to put together a limited EU common foreign and security policy a completely busted flush. The differences over Iraq are acute, but they are the exception rather than the rule: on the majority of foreign policy issues, from the Middle East peace process to the role of international organisations and the value of treaties such as Kyoto, most European countries see eye to eye.

The second is that, for all the harsh words and grandstanding, even in this most contentious area, the EU continues to go about its business in a fairly normal way. As a senior British diplomat puts it: “People are jumpy and everyone feels under pressure, but the EU carries on.”

It is worth saying this if only to counter some currently voguish ideas about the future of Britain's relationship with Europe, encouraged, it must be said, by Tony Blair's portentous remark that there would have to be a “reckoning” after the war. Excited anti-Europeans, for whom the last few weeks have been a delicious vindication, dare to hope that Mr Blair the war leader could soon tread in Margaret Thatcher's footsteps in other ways as well. After all, what did this once most starry-eyed Europhile do when finally forced to choose between Europe and America? Has he not learned, like nearly all of his predecessors, that Britain's fundamental interests and those of its continental “partners” are always doomed to diverge?

Surely, Prime Minister Blatcher will want not only to resist the encroachments of the coming European constitution, but to lead “new” Europe against the integrationist project of the evil Franco-German axis? When it comes to the euro, who would want to share a currency with the cheese-eating surrender monkeys? And while we're about it, what about joining NAFTA?

This is the stuff of fantasy. Mr Blair may have acquired a shrewd appreciation of what the French president Jacques Chirac is about, but for all the tough language he uses these days, he is no Mrs Thatcher. Unlike her, he is instinctively non-confrontational, but more importantly, and also unlike her, he neither feels isolated, nor would relish it if he was. Strange as it may seem, Mr Blair believes, in spite of everything, that there is still everything to play for.

He has a point. Even when it comes to Iraq, Britain has the backing of Spain, Italy, Denmark, the Netherlands and Portugal. As one might expect, a good deal of attention is being paid to keeping this informal alliance in working order. But on the much bigger long-term issue of how Europe should conduct its relationship with America, Mr Blair calculates that it is France that has few real friends. Quite apart from the eight largely pro-American accession countries (to whom Mr Chirac has been so self-destructively offensive), the Irish, the Finns, the Swedes and, up to a point, the Greeks, while uneasy about the war, have shown little interest in the French president's notion of a core group of countries pursuing a form of neo-Gaullism directed from Paris.

From a British perspective, the most interesting question is whether Germany can be detached from the French camp. At present, the chances don't look good. The German foreign minister, Joschka Fischer, has been horrified by what he sees as the bullying and bellicosity of the Bush administration. But privately, Mr Fischer concedes that Europe has no choice other than to have a strategic relationship with America, while the chancellor, Gerhard Schröder is a lonely figure these days, much in need of friends. Despite the electoral popularity of Mr Schröder's pacifism, most of the German political and business establishment is deeply unhappy about being tarred with Mr Chirac's idiosyncratic anti-Americanism. Mr Blair thinks that the Germans may want to move back from the limb they are currently out on. If that is the case, he is keen to help in the difficult job of repairing relations with Washington.

It's a French thing

The problems with France run much deeper. Despite a reasonably cordial 20-minute telephone conversation earlier this week between Mr Blair and Mr Chirac about the war's aftermath, there is great wariness on both sides, which is spilling into the negotiations on the European constitution. A sign of the continuing ill-feeling is that the French are pressing for qualified majority voting on “revenue abatement”—a blatant attempt to sabotage the budgetary rebate won by Mrs Thatcher in the 1980s.

In British eyes, however, there won't be a lot of progress until Mr Chirac faces up to the reality that on the big issue of Europe's relationship with America, he has picked a fight he can't win. “It's a question of whether he actually wants to try and deal with world problems or whether he'd rather just massage his profile at home,” says one British diplomat. One test of that will be if France signs up for the more active counter-terrorism and, particularly, counter-proliferation agenda that Mr Blair intends to urge on the EU.

Mr Blair is not about to turn his back on Europe for a very good reason: he thinks he's winning.

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The changing of the guard

Apr 3rd 2003
From The Economist print edition

After 22 years, Mahathir Mohamad says he is going. His successor must find a way to preserve his achievements but dispense with his authoritarianism, says Christopher Lockwood

Get article background

AS YOU sit over your chicken *rendang*, with perhaps a dish of *kway teoh* lined up for afterwards, the food court on the second floor of the Kuala Lumpur City Centre (KLCC), in the shadow of the soaring Petronas Towers, is a fine place to observe everything that works best about Malaysia. The names of the various stalls—Nasi Padang, Hainanese Chicken Rice, Panggang Delights, North & East Indian Cuisine—are the gastronomic manifestation of Malaysia's extraordinary multiculturalism. Nowhere else in the world can you find the dominant ethnic group (here, the *rendang*-loving Malays, who make up about 53% of the population) living so amicably with such a big and economically powerful minority (the *kway teoh*-eating Chinese, about 26%, not to mention the Indians, another 8%). In 1998, when the Asian crisis sent Malaysia's national income crashing by almost 8%, and next door in Indonesia hundreds of Chinese were being lynched by jealous Indonesians, Malaysia's Chinese went unscathed.

Then there are the women. Many of those who swarm around the KLCC's shops and eateries wear the *tudong*, the local version of the *chador*, tightly framing the face. But the *tudong* is often accompanied by figure-hugging jeans or T-shirts of which the religiously conservative would surely not approve. Nor is there any attempt to impose the *tudong* on non-Muslims, be they the local Chinese or foreigners. Pork and alcohol are freely available.

Exchange rates
Ringgit, March 26th 2003

$1=	3.80	€1=	4.06
¥100=	3.16	£1=	5.98

Nor can the KLCC itself fail to impress the visitor. It is not just the $1,000 jackets at Ermenegildo Zegna, or the 50-inch plasma flat-screen television sets at Sony World, but the quality of the infrastructure: the light railway that glides away to the rest of Kuala Lumpur and connects to a high-speed train that hurtles you out to the gleaming new international airport, 60km (38 miles) away along a cabled-up "Multimedia Super Corridor"; or the bristling forest of skyscrapers, crowned by the needle-thin Petronas Towers, which must rank among the most magnificent office buildings on any continent. It would be easy to imagine that this is the capital of a rich country, not of a developing one with an income of under $4,000 a head.

The ifs and buts

Yet look a little more closely, even here at the heart of Malaysia's success story, and the picture becomes more clouded. Start with those glittering towers. True, one of them is fully occupied, but that is only because Petronas, the government's oil company, has “chosen” to move so many of its staff into it. Petronas reports direct to the prime minister's office, and has often obliged the government before. In 1998, one of its subsidiaries bought out a troubled shipping company that belonged to none other than the prime minister's eldest son, an investment decision that raised more than a few eyebrows. The second tower is half empty, and occupants complain that the offices, especially on the higher floors where the building tapers, are poky and full of awkward corners.

Or take the *tudong*: there are a lot more of them now than there were ten years ago, or even five. Wearing one is not compulsory, but women who immodestly reveal their hair encounter increasing pressure, even abuse. Two of Malaysia's 13 states already have Islamic governments, which are trying to impose laws permitting the amputation of thieves' hands and the stoning of adulterers. They have also cracked down on the sale of alcohol. At national level, the Islamic opposition quadrupled its representation in parliament at the most recent election.

And as for that famous multiculturalism, look again. You will see Chinese and Malays thronging into the food court, but only rarely in mixed groups. And you will probably wait in vain to see a Chinese-Malay couple: they are a rarity, involving compulsory religious education for the non-Muslim partner. The fact is that the two communities, though relations between them are civil enough, live their lives largely apart, attending different schools and universities, speaking different languages and working for different employers. Malaysia's political parties, in practice, are uniformly race-based. The government's vision of a “Malaysian race” by 2020 looks wildly premature.

Malaysia, in short, has achieved remarkable successes, but there is reason to worry that they are not yet solidly bedded down, and they certainly owe more than they should to tough government action. Criticise the policies that have hobbled the Chinese to help the Malays catch up, and you face a charge of sedition. Bring protesters out on the street, and you may be banged up in prison without charge. A proper debate on anything contentious is impossible because the press does pretty much what it is told. Until September 11th 2001, the West regarded Dr Mahathir as something of a pariah because of the heavy-handed methods he employed against his opponents, though the attacks on America have turned him into a necessary ally in the war against terrorism.

How Malaysia stacks up 1

Selected indicators, 2001

	Malaysia	Indonesia	Philippines	Singapore	Thailand
GDP per person, $	3,640	680	1,050	24,740	1,970
Life expectancy, years	71.7	65.9	67.7	78.8	68.9
Health-care spending, % of GDP*	2.5	2.7	3.4	3.5	3.7
Computers per 100 people	13	1	2	51	3
Mobile phones per 100 people	31	3	15	72	12
Electricity (kWh) used per person†	2,474	345	454	6,641	1,352
Cars per 1,000 people*	147	12	10	122	27

Sources: World Bank; World Health Organisation; International Telecommunications Union; International Road Federation

*2000 †1999

Conservative Islam is a looming threat, at least in parts of the country, no matter how carefully government-licensed television stations ensure that all female presenters are *tudong*-less. The imprisonment (usually without charge) of scores of so-called radicals implies either that there is a genuine danger of subversion, which is alarming, or that the government is misusing its emergency powers, which is alarming in a different way. Race relations are mainly good, but there are simmering resentments. And although the economy has bounced back from the dark days of 1997-98, and some of the worst cronyist excesses have been cleaned up, it seems clear that the days of double-digit growth—fuelled by lavish foreign direct investment, most of which has now been diverted to China—are gone for good. The more astute of Malaysia's commentators wonder how the country's 24m people will ever manage to change their status from developing to developed country.

Guardian or jailer?

That is why the transition on which Malaysia is about to embark is so important. In October, if he is to be

taken at his word, Dr Mahathir will step down after 22 years as prime minister, far longer than any democratically elected leader in power anywhere else in the world. His chosen successor, Abdullah Badawi, currently the deputy prime minister, sometimes seems to be everything that Dr Mahathir is not: a cautious bureaucrat rather than a visionary; a conciliator, not a fighter; an unworldly descendant of clerical scholars with a degree in Islamic studies, rather than a technophile and moderniser. Although he is more than a decade younger than his boss, who is a terrifyingly active 77, Mr Badawi appears older and less vigorous. Is he up to the job of guarding Malaysia against the demons of religious extremism, racial hatred and a fragile and volatile global economy? Will he be able to dispense with the authoritarianism that, to many, has made Dr Mahathir look more like a jailer than a guardian of his people? And can he hold the fractious ruling coalition together, a job that even Dr Mahathir has sometimes found a struggle?

Mr Badawi's admirers argue that he is far tougher than he looks. For the past four years he has served as home minister, which means that his name has been on all the orders issued under Malaysia's Internal Security Act, the instrument for rounding up dozens of what the government calls dangerous militants and the opposition calls, for the most part, legitimate opponents. It is not an argument calculated to appeal to western liberals, but it carries some weight.

More palatably, they also say that Mr Badawi is well placed to try to win back support for the ruling party, the United Malays National Organisation (UMNO), which has been leaching away to the main Islamic opposition party, PAS. Thanks to his own religious qualifications, Mr Badawi can speak with greater authority—in Arabic if need be—than Dr Mahathir does in defence of the government's secular version of Islam against PAS's charges of godlessness. Mr Badawi's modest private life and generally clean image may also go down well as a change from his predecessor, who is famous for spending hundreds of millions of dollars on dubious “megaprojects”. These include Kuala Lumpur's half-empty new international airport, the Multimedia Super Corridor between the airport and the city, and the glittering new administrative capital he has built in Putrajaya, just outside Kuala Lumpur, complete with an over-the-top prime minister's palace which Mr Badawi would be well advised not to move into.

The smarter among Mr Badawi's suppporters concede that cleaning up politics—or at least the perception of politics—will be their most pressing task come October. Mr Badawi has put together an impressive team of bright young people to plan for the handover, but the timing will be tight. A general election must be held by the end of 2004, and a poor result would spell an early end to Mr Badawi's prime ministership. UMNO politics are a snake-pit, as often happens when one party has monopolised power for

too long, and at least two powerful challengers are already lining up. Above all, the election result will depend on how well Mr Badawi tackles the Islamic opposition.

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The greening of Malaysia

Apr 3rd 2003
From The Economist print edition

The government's first priority is to prevent the Islamic opposition from making further gains

Reuters

A WORLD away from the hillside palace Dr Mahathir has built himself in Putrajaya lives the man the ruling party fears most. Nik Aziz, the 71-year-old spiritual leader of the Parti Islam Semalaysia (PAS), the main Islamic opposition party, inhabits the same two-storey wood and brick building by the local mosque that his father did before him, even though, since 1990, he has been chief minister of the state of Kelantan, in Malaysia's poor north-east. His conspicuously simple clothes, the obvious devotion of his followers (who call him Tok Guru, meaning something like “Uncle Teacher”) and his genuinely friendly and hospitable manner all contribute to his air of saintliness. Only the enormous black Mercedes—a recent acquisition—parked outside the Mosque strikes a jarring note.

UMNO, the party of all of Malaysia's prime ministers and the core of the ruling Barisan Nasional (BN, or National Front) coalition, has good reason to fear PAS, which three years ago gave it the worst scare in its 56-year history. In the election in November 1999, PAS gained 20 seats, mainly at UMNO's expense. Thanks to Malaysia's first-past-the-post electoral system, the overall result still left the BN overwhelmingly in control, with 148 of the 193 seats, but that comfortable figure concealed some much more worrying ones. The BN won only 56.6% of all votes cast, down seven percentage points, with the rest going to a newly formed “Barisan Alternatif” that grouped together PAS, the mainly Chinese Democratic Action Party (DAP) and the new, mainly Malay National Justice Party (Keadilan), led by Wan Azizah, the wife of the sacked and jailed former deputy prime minister, Anwar Ibrahim.

The result implied, for the first time, that UMNO no longer commanded a majority of the Malay vote. And even though the Barisan Alternatif has since disintegrated, its constituent parties have pledged to continue the election pact under which the parties agree to stand down their candidates in favour of the strongest among them. Even more humiliating for UMNO, PAS took control of a second state, Terengganu, alongside Kelantan, and made inroads in Kedah, Perak, Perlis and Pahang, which are all now potentially vulnerable, and even in UMNO heartland states like Selangor. UMNO responded by stripping Terengganu's state government of the royalties from offshore oil drilling on which its finances depended.

The Barisan Alternatif may have helped to give it a veneer of respectability, but there is nothing moderate about the version of Islam that PAS espouses. Its political leader, Hadi Awang, declared a *jihad*, or holy war, against UMNO as early as 1986, denouncing the party as un-Islamic. More recently, PAS leaders have declared *jihad* against America. During the campaign in Afghanistan, PAS supporters demonstrated outside the American embassy in Kuala Lumpur, wearing Osama bin Laden T-shirts. America is far and away Malaysia's largest trading partner, but that has not stopped PAS from calling for a boycott of American goods. Nik Aziz says he believes that the destruction of the World Trade Centre was carried out by Jews, not al-Qaeda. But perhaps most striking is the PAS leadership's enthusiasm for cutting off hands.

Malaysia has always lived under *shariah*, or Islamic law, but its scope has been tightly circumscribed since colonial times. It applies only to Malays, and then only in civil matters and to relatively minor criminal ones, for which the sentence is not more than a year in prison, five strokes of the rattan or a fine of 3,000 ringgit. All serious criminal matters are the province of the federal government. But Nik Aziz in Kelantan and Hadi Awang, chief minister in next-door Terengganu since the 1999 election, have brought forward bills that would impose *hudud*, the strict and non-discretionary Islamic list of penalties including amputation of a hand for theft, death by stoning for adultery and 100 lashes plus a year in jail for sex between people not married to each other.

These laws are not supposed to apply to non-Muslims, although some PAS leaders say that they may in time be extended to them. For Nik Aziz, it is simply unthinkable not to have such punishments on the books. “An Islamic state must be guided by the Koran and the Hadith,” he says. “If we do not have *hudud*, what kind of an Islamic state are we?” Western horror, he thinks, is misplaced. “On drugs, we are very tough: we have the death penalty, and you don't mind at all. But when we propose the cutting off of hands, you get very upset. Yet chopping hands isn't as serious as taking someone's life.”

How much hudud?

So far, the *hudud* laws have not been applied: the federal government has refused to approve them, and the police in the two PAS states say they will not enforce them. But the PAS leaders mutter about recruiting their own *hudud* police and defying the federal government, though many believe this is bluster: PAS often shrinks from actually practising what it preaches. Still, alcohol has largely vanished from PAS-ruled states, and pop concerts are banned, as is traditional Malay *mak yong* dancing, because it involves men and women dancing together. The lights are no longer dimmed in cinemas, to prevent the offence of “close proximity”.

Not all PAS members are as fundamentalist as the two chief ministers: indeed, there is a sharp division between them and a younger group educated at European rather than Middle Eastern universities. But for now, at least, it is the fundamentalists who have the upper hand.

If recent by-elections are any guide, none of this seems to have done much damage to PAS's popularity. In July 2002, following the death of Fadzil Noor, then the PAS political leader, UMNO saw its opportunity to beat PAS back. It threw everything it had into the by-election, including allegations of links between PAS and a banned Islamic militant group, the KMM. But those allegations cannot be verified, because the 70-plus alleged KMM members are being detained under Malaysia's Internal Security Act (ISA), which dispenses with the need for evidence, a trial or even a charge. One of those being held is the son of Nik Aziz, though what he is supposed to have done is a mystery.

UMNO was fortunate in that the seat in question was in Kedah, Dr Mahathir's home state, and it needed to overturn a majority of just 2,900. In the event, it did win, but by only 283 votes; and it failed to win the separate election for Fadzil Noor's seat in the state parliament. This hardly bodes well for its fight-back from its 1999 decline, which it attributes to the economic crisis and the aftermath of Anwar Ibrahim's arrest.

Mr Anwar was a pioneer of Malaysia's Islamic Youth Movement, until Dr Mahathir co-opted him into UMNO in 1982, and he retains a strong following among the religious. His arrest, and above all the beating he received in prison, undid at a stroke much of the gain from 16 years of careful cultivation of Malaysia's moderate Islamists. If, as the government's supporters contend, its fortunes have greatly improved since then, it should have done much better in Kedah.

Much of PAS's success is undoubtedly a reaction to UMNO's unpopularity, and PAS has successfully hammered away at allegations of corruption, of excessive spending on Dr Mahathir's beloved megaprojects and of state-funded bail-outs for favoured captains of industry while others were going to the wall. UMNO's more honest thinkers admit there is much truth in all this, and are hoping for reform under Mr Badawi. But a large part of PAS's appeal also stems from the fact that it is an uncompromisingly Islamic party, which poses a much more intractable problem for UMNO. Should it take a stand against the Islamisation of a country that has always prided itself on its secular nature (something of a necessity, given that only 60% of the population is Muslim)? Or should it compete directly with PAS, by offering its own, rival version of Islam? UMNO's solution has been a blend of both.

In Malaysia, Islam sells. There are reckoned to be around 700,000 young Malays attending religious schools in the country, and many more studying abroad in such Islamic centres as Pakistan, Egypt and Saudi Arabia. Many, though by no means all, of these schools are overtly political. And although religious extremism is nothing like as much of a problem as in neighbouring Indonesia, at least

until 2001 extremists have seen Malaysia as an ideal place to operate from. Riduan Isamuddin, also known as Hambali, is South-East Asia's most sought-after terrorist suspect, wanted in connection with a string of bombings, including last year's Bali bomb. In the early 1990s he was based at the Luqmanul Hakiem religious school in southern Malaysia's Johor state. So, too, was Abu Bakar Basyir, alleged to be the leader of Jemaah Islamiah, which is thought to have carried out the Bali attack, and Mukhlas, alleged to be its operations chief.

Almost no contest 2

Malaysia's parliament, lower-house seats
1999 election

State	BN	PAS	DAP	Keadilan
Johor	20	-	-	-
Kedah	7	8	-	-
Kelantan	1	10	-	3
Kuala Lumpur*	6	-	4	-
Melaka	4	-	1	-
Negeri Sembilan	7	-	-	-
Pahang	11	-	-	-
Perak	20	2	1	-
Perlis	3	-	-	-
Pulau Penang	6	-	4	1
Sabah†	18	-	-	-
Sarawak	28	-	-	-
Selangor	17	-	-	-
Terengganu	-	7	-	1
Total†	148	27	10	5

*Federal territory †Does not include 3 seats won by PBS
BN=Barisan Nasional (National Front)
PAS=Parti Islam Semalaysia (Pan-Malaysian Islamic Party)
DAP=Democratic Action Party
Keadilan=Natural Justice Party
Source: Election Commission of Malaysia

That school has now been closed, making Dr Mahathir the only leader in Asia who has been brave enough to take on extremism at source. At least 500 other Malaysian religious schools face the same fate, because last October the government started withdrawing state funding from such establishments. “The majority of these schools contribute nothing to the educational stock,” says Mr Badawi. Human-rights activists have objected that the government's de-facto censorship of classes and sermons amounts to a violation of religious freedom, but the government seems little concerned. A more serious worry may be that, deprived of government funds, the religious schools will be forced to look for money from abroad, which will inevitably come with ideological strings attached.

There have also been scores of arrests of suspected militants: according to one human-rights group, 113 people are being held under the ISA in Malaysia's main detention camp alone. September 11th, in a way, has been a godsend to Dr Mahathir, allowing him to crack down on “extremists” without a peep of protest from the West, even if some of them are merely opponents of the government. By trying to link those arrested to PAS, the government has hoped to discredit the opposition, though it is not clear that this has worked. But Dr Mahathir's willingness to take on the militants long pre-dated September 11th: the first big sweep was in July 2001, well before the World Trade Centre fell.

Because, under the ISA, no one ever needs to be put on trial, it is difficult to say whether violent Islam is a big problem in Malaysia. But most observers seem to think that it is quite limited, and that the government now has it firmly under control. PAS's brand of Islam is entirely different: democratic, non-violent and much harder for the government to deal with.

Reuters

Mahathir's magnificent mosque

The second strand of the government's policy for dealing with the PAS is to pre-empt it. For the past 20 years, Malaysia has been growing steadily more Islamic. The signs of it are everywhere, perhaps most glaringly at shiny new Putrajaya, where Dr Mahathir ordered the construction of an immense mosque with a minaret 116 metres (380 feet) high, the tallest in South-East Asia. For a country that insists on its multiculturalism, this is an odd signal to send to the 40% of the population who are not Muslims.

The government has also worked tirelessly to encourage Islamic banking, to the extent that even foreign banks are obliged to provide Islamic banking services. Since 1998, Islamic civilisation has been a

compulsory subject at Malaysia's national universities. There is a new Islamic university, and attending religious classes is a regular feature of life in a government office. Two years ago the government introduced a law that obliges anyone who plans to become an apostate (an Islamic woman, for instance, who wants to marry a Chinese man, rare though that is) to spend a year in a religious re-education camp. That is less draconian than PAS's proposed punishment of death, but it is another step in a disturbing direction.

The most debated sign of this Islamisation drive came from the prime minister himself, who on September 29th 2001 said that Malaysia is “an Islamic state”. But what did that mean? To his ethnic Chinese critics in the opposition DAP, it was little short of a declaration of cultural war. All previous prime ministers had been careful to call Malaysia a secular state; although Islam is recognised as “the religion of the federation”, the constitution pledges that other religions may be practised “in peace and harmony”. For their pains, 33 of the DAP activists who protested at the speech were (briefly) arrested, including the party's leader. According to UMNO, all Dr Mahathir meant was that Malaysia is already Islamic enough, and needs to make no further moves towards theocracy, but the phrase sent shivers down Chinese and Indian spines. PAS, for its part, dismissed it as inadequate.

For all that Islamisation, it is worth recalling how secular Malaysia remains. Alcohol is freely available everywhere except in the two PAS-governed states. Chinese restaurants cheerfully sell pork, though when they share premises, as in hawker centres or food courts, they must stick with *halal* food. The *tudong* is still a matter of choice, more or less. Women are highly emancipated and eligible for top jobs. For example, the governor of the central bank is a woman, as is the minister for trade and industry. And although laws against “close proximity” are on the books everywhere, they are seldom applied, and do not seem to interfere with Kuala Lumpur's reasonably lively night-life.

Election fever

Panos

KL's secular pleasures

How will the issue of religion play at the next election, which is probably less than a year away? One factor is that there will be 2m new voters, an extraordinary number for a population of only 24m. The young in Malaysia, as anywhere else in the Islamic world, tend to be far more religiously radical than their elders.

If the election were a straight fight for the Malay vote between PAS and UMNO, things might go badly for the government, but Malaysian politics do not work that way. The contest is not so much among parties as among shifting coalitions, whose membership is never fixed for long. The genius of UMNO, and the reason why it is still in power after an unbroken run of 45 years, is that it has always managed to co-opt the people it needs. Even PAS was part of the BN between 1974 and 1978.

At present, besides UMNO the Barisan Nasionalincludes the Malay Chinese Association (MCA), Gerakan (a mainly Chinese left-leaning party) and the Malaysian Indian Congress, as well as ten smaller parties, including the vitally important dominant parties in the East Malaysian states of Sarawak and Sabah. These last two states, which are mainly Christian, fond of rum and unlikely ever to vote for PAS, deliver a useful 49 seats to the ruling coalition. On top of that, according to A.B. Shamsul, professor of social anthropology at the National University of Malaysia, the presence of the MCA in the ruling coalition more or less guarantees that, in all except the smallish number of seats where the population is more than 70% Malay, PAS is bound to lose. Few, if any, Chinese or Indians are ever going to vote for a party that wants to see full-blown *shariah* become the basis of law.

True, PAS has had a Chinese partner, in the shape of the DAP, in its own Alternative Front coalition. But the DAP saw its vote bleed away to the MCA, because its voters distrusted PAS, and in 2001 it withdrew from the coalition. So with the Malay vote split more or less evenly, and the bulk of the Chinese vote sewn up, the BN looks invincible wherever non-Malays are present in reasonable numbers. According to one governmentinsider, the latest changes to Malaysia's electoral boundaries, which will add 25 seats, are designed to ensure that Malay and non-Malay voters are well mixed. That is no doubt good for multiculturalism. But it means that PAS's chances of breaking through at the national level are negligible, particularly following the disintegration of the Alternative Front. Still, were the Islamists merely to capture another state, let alone two, the damage to UMNO's prestige would be immense. How likely is

that to happen? In part, it depends on how far Mr Badawi's new government can show that it is breaking with Dr Mahathir's dictatorial leanings.

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A tale from Terengganu

Apr 3rd 2003
From The Economist print edition

Can PAS win Chinese hearts?

SINCE Malays make up only 53% of Malaysia's population, any party that wants to wield power needs the support of the non-Malays, and in particular of the Chinese, the largest and by far the wealthiest minority. That is why the state of Terengganu is so important to PAS, which won it three years ago. The party needs to reassure the Chinese that they can prosper under its rule.

Up to a point, it is succeeding. Stroll around the main shopping street in the centre of Kuala Terengganu, the state capital, and the Chinese seem to be thriving. By far the greatest concentration of shops and restaurants is to be found in Kampong Cina (Chinatown), and if you fancy a beer or a plate of sweet-and-sour pork, it is readily available. The rest of the state, however, is now almost completely dry. And a recent PAS ordinance has decreed that tour guides may not escort people of the opposite sex, so that a family out to see the sights has to divide into a male and a female group and hire two guides.

However, Ng Chai Hing, a DAP local councillor, says that the PAS authorities have efficiently wooed the Chinese community, giving assurances that the *hudud* laws will not apply to it and, in one much-appreciated case, giving land title to a group of Chinese families who had been appealing in vain to the previous, UMNO-led, state government for 30 years. Indeed, according to one school of thought PAS might suit the Chinese community better than UMNO. A main plank of UMNO's political platform has been to increase Malays' share of the economic pie, invariably at the expense of the Chinese. The Islamists, by contrast, are content to leave well alone.

But it is difficult to generalise from Terengganu to the rest of the country. The state's Chinese population is in a tiny minority of 3-4%. It has been there for almost 300 years, and has long learned to live in an overwhelmingly Malay, Islamic environment. A PAS-dominated government in Kuala Lumpur in charge of a genuinely Islamic state would be a very different matter. Non-Muslims could not be lawyers or political decision-makers, and their testimony in court would be worth only half that of Muslims. In Terengganu or anywhere else in Malaysia, the Chinese would find that hard to live with.

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Anwar Ibrahim's long shadow

Apr 3rd 2003
From The Economist print edition

The brutal treatment meted out to the former deputy prime minister stills haunts Malaysian politics

AP

Anwar (and wife, right) in happier days

APPOINTING an official human-rights commission seemed a good idea at the time, but when the creature started showing signs of independence, the Malaysian government had to act. It declined to renew the appointment of its most troublesome members and, to be on the safe side, put in a former attorney-general (of all people) as chairman. Small wonder that Malaysia's human-rights NGOs boycotted the commission for much of last year.

The story illustrates a depressing trend under Dr Mahathir: wherever possible, criticism of the ruling party is choked off at source. Malaysia may be a democracy in broad outline, and opposition parties do win seats in parliament, but only against great handicaps. Freedom of expression has been badly eroded under Dr Mahathir, and critics of the government no longer believe that they can count on either the media or the courts to protect them.

The press is the most obvious example. With the exception only of Myanmar's, it is the most supine in non-communist Asia. The leading paper, the *New Straits Times*, is almost as fawning a read as the *China Daily*, invariably devoting slabs of uncritical coverage to the sayings and doings of Dr Mahathir and now Mr Badawi. *Reporters sans Frontières*, which works for freedom of the press, last year ranked Malaysia 110th out of 139 countries on that score.

Unwelcome views are squeezed out by a variety of methods. The *Star*, which once had a reputation for independence, was closed down for a year in 1987 for criticising a wave of arrests, and has been a shadow of its former self ever since. PAS's party newspaper, *Harakah*, and the DAP's *Rocket* can be sold only to party members, and *Harakah* has been ordered to distribute only fortnightly, not twice a week. A DAP party newspaper in east Malaysia has been trying in vain to get a licence to print for the rest of the country. Two main Chinese-language dailies, the *China Press* and *Nanyang Siang Pau*, which used to be considered less captive than the Malay-language press, were bought by the Malaysian Chinese Association, part of the ruling coalition, in 2001. And the less said about Malaysian television, the better.

Protest in cyberspace

Only the internet has provided a little relief from the dreary tide, though, sadly, few people have taken

advantage of this, with the honorable exception of *Malaysiakini*, a web publication run by the courageous Steven Gan. Their caution was vindicated when in January police seized *Malaysiakini*'s computers after it published a letter criticising the pampering of Malays. The website stayed up, operated from a back-up site, but in skeletal form. The government makes no apology for this kind of behaviour, claiming the right to supress comment which might disturb Malaysia's delicate racial balancing act.

The opposition cannot even hold rallies, because in July 2001 the government imposed a blanket ban on political gatherings in public places, supposedly in the interest of public order. The opposition says this hurts it far more than UMNO, which can get its message across through the compliant media. Supposedly, indoor gatherings are fine, except that if they are organised by opposition parties, the police sometimes block those too.

By far the most serious cause for concern, though, is the government's misuse of the Internal Security Act (ISA), a draconian piece of legislation enacted shortly after independence. Most of the arrests under the ISA have been of alleged Islamic militants, for which there is currently a degree of international sympathy. But in April 2001, the government put behind bars a group of activists including prominent members of the mainly-Malay opposition group Keadilan, founded in protest at the jailing of Anwar Ibrahim.

UMNO apparatchiks mutter darkly that the "*Reformasi* Six"—the others have since been released—had been planning to overthrow the state, though the evidence for this has never been presented. What is certain is that the arrests have deprived Keadilan of some of its most able people. The party once looked like a credible threat to UMNO, appealing to educated, urban voters who were disenchanted with Dr Mahathir's autocratic style. It also offered a counterbalance to PAS, which is predominantly rural. But with many of its leaders in prison, and rallies outlawed, it has been largely neutralised.

At a minimum, human-rights campaigners want safeguards introduced into the workings of the ISA. As things stand, ministers have almost unfettered discretion to hold suspects for an initial 60 days, followed by two more years: when that time is up, a fresh arrest can be made.

What really shocked observers both inside and outside Malaysia, however, was the case of Mr Anwar, the most charismatic young politician of his generation, who was being groomed to succeed Dr Mahathir. The reasons for the falling out are a matter of debate. The Mahathir camp says it was pure impatience on Mr Anwar's part. Mr Anwar's wife, Wan Azizah, who now leads Keadilan, says there were disagreements over how to handle the economic crisis and over Dr Mahathir's lavish spending on his mega-projects. Either way, in September 1998 Mr Anwar was sacked.

Mr Anwar did not go quietly. At the time, South-East Asian politics were running hot: in Indonesia, General Suharto had been driven from power four months earlier by huge street demonstrations. By calling his supporters on to the streets, and using some of the same slogans, Mr Anwar seemed to be posing a serious threat to the government. It did not come as a great surprise when, on the night of a vast demonstration, Mr Anwar was arrested. Nine days later, he was charged not with public order offences but with sodomy and corruption, witnesses having conveniently come forward years after the alleged events. Mr Anwar was found guilty on both counts. Human-rights campaigners think the trial was farcical. Mr Anwar is now serving consecutive six- and nine-year prison terms. As this survey went to press, Mr Anwar's appeal against the second conviction was, at long last, being heard. Theoretically, he could be released as early as April 14th, though few observers expect that to happen.

The treatment meted out to Mr Anwar still rankles with many. He was badly beaten up in prison, and the police chief responsible was given a sentence of only two months. But September 11th changed a lot: before then, the Bush administration regarded the Anwar issue as an obstacle to the Malaysian prime minister meeting the American president, but in May 2002 Dr Mahathir visited the White House.

Still, the domestic element matters, too. How Mr Badawi deals with Mr Anwar will be seen as an important test of his prime ministership. Whatever happens, it seems certain that Mr Anwar, arguably as brilliant and controversial a figure as Dr Mahathir himself, will be heard from again.

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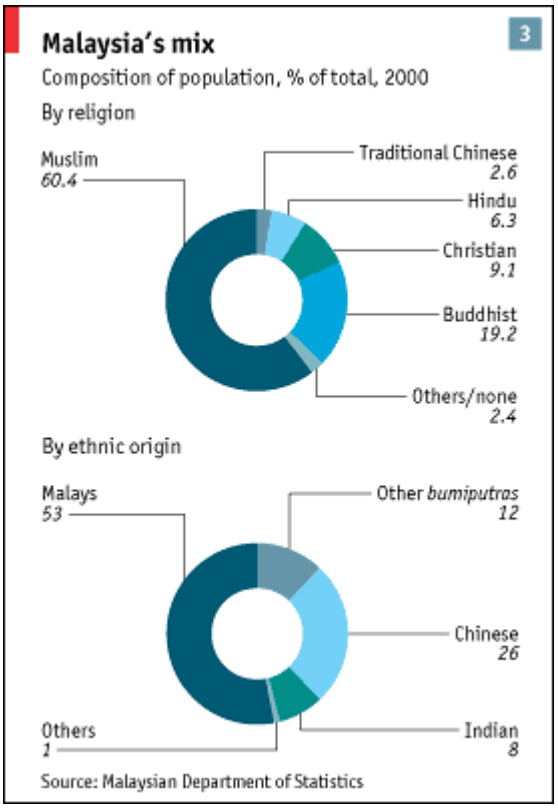
The slaughter of sacred cows

Apr 3rd 2003
From The Economist print edition

Some cherished policies are being re-examined



IS DR MAHATHIR an old man in a hurry? It certainly seems so. With his long reign drawing to a close, he has been reversing some of his party's most cherished policies, perhaps secure in the knowledge that it is his successor who will have to deal with any backlash.

Malaysia is probably the only country in the world with racial discrimination explicitly written into its constitution. The Malays—or to be more accurate, the *bumiputras*, or "sons of the soil", a term that covers not only the Malays but other indigenous ethnic groups as well—felt themselves at a serious disadvantage when independence came in 1957. Under British protection, Malaysia's Chinese traders and businessmen had prospered. The *bumiputras*, who lived mainly in the rural areas and had little access to education, owned only 2.5% of the country's corporate assets, against over 30% for the Chinese. (Foreigners, mainly British, owned the rest.)

On May 13th 1969, simmering tension between the Malays and the Chinese burst on to the streets. By the end of that day, 200 people were dead, and Malaysia was on its way to adopting a wide-ranging policy of positive discrimination. Launched in 1971, the New Economic Policy (NEP) reserved the lion's share of government jobs and university places for *bumiputras*. Publicly quoted companies had to ensure that at least 30% of their shares were held by this group, and to hand out a similar share of jobs to them. At the same time the government "Malayised" education: Malay schools had to teach solely in Malay, not English, though Chinese-language primary schools, paid for by the government, and Chinese secondary schools, mainly funded by the Chinese community, were allowed to continue as before.

These policies have had a big impact, not all of it as planned. Counterproductively, the education provisions have kept Malay and Chinese children apart, because they are educated in different establishments and in different languages. Not many Chinese go to the national universities either, partly

because of the language issue, but mainly because there is a quota system. Although this has been relaxed in recent years, so that only 55% of places are now reserved for *bumiputras*, the Chinese are far more likely to send their children to university, so a Chinese student needs much better grades to be sure of a place. The solution until recently has been for tens of thousands of young Chinese Malaysians to be sent to study abroad, at great expense. For the Malays, the consequent decline in the standard of English has become quite marked.

The NEP and its successor plans have also left their mark on business, again not quite as intended. Chinese companies have, by and large, chosen to stay small and private, rather than growing to the point of having to comply with the NEP's requirements. At the same time, the encouragement given to Malay businessmen has led to some spectacular and expensive misjudgments. Critics argue that the NEP promoted crony capitalism (see article), with asset sales, cheap credit and large contracts being directed to a favoured few ethnic Malays. The Asian economic crisis in 1997-98 exposed the consequent weaknesses.

Learning to love the NEP

Even so, it appears that Malaysia's Chinese have come to accept the NEP. For all its limitations, the Chinese in Malaysia think themselves better off than in neighbouring Thailand or Indonesia, where they had to assimilate completely. In Thailand, they were forced to take Thai names: if you did not know that, you might think there were no Chinese in Thailand at all. In Indonesia, most manifestations of Chinese culture (though not names) were suppressed: at one time, it was illegal to import Chinese books or papers. Even so, Indonesia experienced repeated pogroms. “If the NEP is the price we pay to keep our culture and live safely, it is not a bad price,” says one Chinese businessman. “The policy has actually helped us,” argues Ng Lip Yong, a Chinese member of parliament. “It has made us more resilient, more competitive. We have had to fight the handicaps, and it has made us tougher.” No business could sound more Malay than Royal Selangor, Malaysia's famous pewter-maker, but it is owned and run by a Chinese.

Politically, too, the Chinese are well placed these days. The success of the PAS Islamists has meant that, in effect, the Chinese (and other non-Malays) hold the balance of power between the two big Malay parties, PAS and UMNO. Ling Liong Sik, the leader of the Malaysian Chinese Association, which is part of the ruling coalition, says that his members are less bothered about the restrictions than they used to be. No Chinese, for instance, would want a civil-service job anyway, and there are now so many private universities in Malaysia that would-be Chinese students no longer have to go abroad.

In any case, the days of the NEP now appear to be numbered. In a famous book published in 1970, “The Malay Dilemma”, Dr Mahathir, who had just been expelled from UMNO for criticising the leadership, argued that Malays had to decide “whether they should stop trying to help themselves in order that they should be proud to be the poor citizens of a prosperous country, or whether they should try to get at some of the riches that this country boasts of, even if it blurs the economic picture of Malaysia a little”. In the 1970s, UMNO chose the second of those options. But Dr Mahathir called it a dilemma advisedly, and it seems that he still sees it as one. At any rate, the first option now seems to be finding increasing favour.

For the past couple of years, Dr Mahathir and Mr Badawi have been calling on Malays to “throw away their crutches”. If anything, Mr Badawi believes this even more strongly than his boss. In 2000, he was the first to break the taboo, describing the NEP as “mollycoddling”, and extolling the virtues of competition. Mr Badawi says that *bumiputras* now own 23% of Malaysia's assets. That is less than the 30% target that was supposed to be achieved by 1990, but the government seems to think that discrimination has done its work.

Rules are for bending

The relaxation of the university quota is one sign of this, but there are others. In high-tech, for instance, the terms of the NEP do not apply to the huge area designated by the government as a Multimedia Super Corridor, where all sorts of tax breaks are available. In principle, most public businesses, for instance stockbrokers, have to ensure that 30% of their staff are *bumiputra*. “In practice, it isn't really like that,” says one broker. “I go along to the central bank, and I show them that we have advertised for *bumiputra* stock analysts, but that we haven't been able to find any with the right qualifications. They never actually fine us.”

Even the requirement that 30% of a firm's equity be held by *bumiputras* is not as arduous as it seems. For instance, it does not apply to foreign firms manufacturing for the export market. And where it does apply, these days an increasing number of well-managed *bumiputra* firms can be drawn in as partners.

None of this is to suggest that race relations in Malaysia are perfect: far from it. It seems invidious, for example, that Malaysia's political parties are all race-based (a few of the small parties claim to be otherwise, but Keadilan is overwhelmingly Malay, Gerakan and the DAP are overwhelmingly Chinese).

The past year has also seen a first-class inter-racial row on the subject of schools. It is difficult to overestimate the importance of education in Malaysia, because it cuts to the heart of both religious and racial tensions. That is why the job of education minister, considered something of a backwater in most countries, carries huge weight in this one. Dr Mahathir once held the job, as did his predecessor as prime minister, Hussein Onn. Anwar Ibrahim held it, and so did Mr Badawi. The latest dispute was over another of Dr Mahathir's attempts to unravel a cherished policy from the past: the teaching of English. This year marked the start of the re-introduction of English as a language of instruction in Malaysia's primary schools, to the vigorous opposition of nationalist Malays and Chinese alike. Dr Mahathir inherited the Malay education policy, as he did the NEP, when he became prime minister in 1981, but has felt bold enough to change it only towards the end of his long tenure.

In the event, the loudest protests came from the Chinese, whose schools have had to fend off many assaults on their independence, and the government had to give ground to them. Maths and science classes in Chinese primary schools will continue to be taught mainly in Chinese, though there will be extra tuition in English in those subjects. To the MCA and Gerakan, this demonstrates that being inside the BN coalition confers real benefit, and that the Chinese are becoming more equal.

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The big clean-up

Apr 3rd 2003
From The Economist print edition

Malaysia has made a good job of putting its house in order after the Asian economic crisis

THERE are some advantages to democratic dictatorship as practised in Malaysia. If necessary, a government can take action with a degree of dispatch that leaves more pluralistic polities for dead. After Asia's economic crisis in 1997-98, weak governments in Thailand and the Philippines dithered, and Indonesia seemed paralysed by the fall of Suharto. By contrast, Malaysia moved swiftly to reform itself, and by general agreement has done much the most effective clean-up job of any of the South-East Asian countries.

Crucially, it got a head start. In May 1998, when the stockmarket was still only 7% off its peak and non-performing loans (NPLs) were around 7% of all loans, the government decided to set up an asset-management company to tackle the worst cases. By July that year the legislation had galloped through parliament, and by August the agency, Danaharta, had started work. Thailand's equivalent did not get going until 2001.

By any account, Danaharta has been a success. As the crisis deepened, some 20% of Malaysian debt was reckoned to be non-performing. Danaharta took on half of that, mainly the largest, most problematic loans. The easy part was buying the debt from the banks, which Danaharta did at market prices (on average, at a discount of 54% to face value). The hard part was to force the companies owing the money to retrench and liquidate assets to pay Danaharta back, or to restructure so that the debt could be returned to the market. Leaving aside a legal hiccup, now under appeal to the Federal Court, Danaharta seems well on the way to success. It expects to be able to get 57% of the value of its acquired and managed loans back, and may even make a small profit. It still plans to close down in 2005, as originally envisaged.

Another government body, the Corporate Debt Restructuring Committee, charged with resolving syndicated debt, has already closed its doors, on schedule in July 2002. Less than 8% of Malaysia's debt stock is now non-performing to the extent of being six months or more in arrears. Azman Yahya, still under 40, has run both bodies, having previously worked in the private sector. He attributes Danaharta's success to the relative independence from government and the sweeping powers it was given. It has run itself exactly like a private-sector outfit, with a board that includes two foreign bankers.

Bank restructuring has been another part of the clean-up. The government injected a total of 11 billion ringgit into Malaysia's banks, in part to help them over the shock of having to sell their debt well below book value. In return, they had to accept a wave of consolidation. A total of 71 lending institutions have been consolidated into ten “anchor” banks (and another 20 specialist financial institutions). This is still too many for a country of only 24m people, and a further wave of mergers is being encouraged. But competition in the banking sector is not being allowed to go too far. Zeti Akhtar Aziz, governor of the Bank of Malaysia, the central bank, says she would not want foreign banks to gain more than half the Malaysian market. Foreign banks face formidable restrictions, even down to the number of counters they are allowed to operate, or the speed at which they were allowed to introduce internet banking (Malaysian banks were given a one-year head start).

Azman sees a culture change

It all looks good on paper, but question-marks remain. Will the government-backed rescues create a climate of moral hazard, so that, in a few years, debts will be piled up as incautiously as before? No, reckons Mr Azman. Malaysia's business culture has been fundamentally changed. For instance, listed companies are now required to separate the functions of owner and chief executive. They must also submit quarterly results to the stock exchange, complete

with balance sheets and profit-and-loss accounts. These are tougher requirements than elsewhere in South-East Asia. Nor, he insists, were there any bail-outs. The banks took a big hit when Danaharta took over their loan accounts at market, rather than face, value. The experience, he says, will make them more cautious about whom they lend to in future.

A lesson learnt?

Abdul Aziz, who runs the Malaysia office of Transparency International, an organisation dedicated to fighting corruption, agrees—up to a point. Some of the most reckless borrowers in the pre-crash days have indeed lost their jobs, he concedes. The two most notorious of these are Tajudin Ramli, who headed MAS, Malaysia's airline, and Halim Saad, at the conglomerate Renong. Both men fit the classic mould of government crony: both were protégés of the then finance minister, Daim Zainuddin; both are Malays, boosted to create role-models for the *bumiputras*, who turned out to be anything but. But, according to Abdul Aziz, Tajudin Ramli received a huge farewell present from the government even as he was being shunted out of the door. His 29% stake was bought by the government for 1.8 billion ringgit, close to three times the market price.

And at Renong, the government stepped in when the flotation of a telecoms subsidiary went badly wrong. Still, says Abdul Aziz, “on balance, they seem to have learned a lesson. We simply cannot afford a repetition of 1997-98.” The “resignation” of Mr Daim in July 2001 is said by some analysts to have marked a break with the old culture of cronyism. Others argue that Mr Daim may indeed have been the crony-master, but could hardly have been acting without the approval of Dr Mahathir.

That raises the question of whether cronyism really is dead, or whether fresh cronies are popping up to take the old ones' places. The best guess is that cronyism has not gone away, but that it is probably less rampant than before. One man in particular, though, fits the description of a crony perfectly: Syed Mokhtar al-Bukhary. Mr al-Bukhary, a close friend of the prime minister's, has built an extraordinary empire in a the five years since the crisis, including Malaysia's fast-growing new container port at Tanjung Pelepas, a hotel and property group, Pernas, mining companies, power companies, palm-oil companies and much else, including a controlling stake in the Bakun dam on the island of Borneo.

Reuters

Zeti, chief broom

Mr al-Bukhary is a proven achiever (as, though, were Tajudin Ramli and Halim Saad in their day), and Tanjung Pelepas is a remarkable success story, having attracted the regional hub operations of Denmark's Maersk and Taiwan's Evergreen away from Singapore. But there are worries. Mr al-Bukhary never gives interviews, and shrouds his affairs in secrecy: all his assets are held through complex vehicles. Several of the formerly state-controlled assets he acquired did not go through the normal tender process. Analysts fear that, just like other Malay “winners” picked by the government in the past, Mr al-Bukhary may already have over-extended himself: the Bakun dam, in particular, is an expensive gamble, and Tanjung Pelepas is unlikely to start making money until 2005.

There are other alleged cronies, but none of them is as mysterious or as all-embracing. And neither of the other two most prominent ones, Ananda Krishnan and Francis Yeoh, are *bumiputras*. Dr Mahathir's supporters argue that such men are not cronies, merely successful businessmen, and that the concentration of contracts in their hands simply reflects the fact that the pool of available talent is relatively limited. They may have a point.

Overcoming the Asian crisis was about more than just restructuring and house-cleaning, of course. Another big part of it was the imposition of capital and exchange controls and the introduction of a dollar peg for the ringgit. All of these were greeted with horror by the international community at the time, and Dr Mahathir's government was deeply divided over them. Since then the criticism has turned to grudging approval. Even the IMF, at the time the harshest critic of Dr Mahathir's medicine, praised Malaysia's economic recovery in a 2001 report. That said, wariness remains: foreign portolio investment in Malaysia has never returned to anything like pre-crisis levels, though measures freeing up the capital markets, announced on March 11th, may help.

Also crucial to the recovery has been the peg. From a rate of 3.4 ringgit to one dollar, the currency was

devalued to 3.8, well below the then market rate, so investors had little incentive to take their money out by illicit means. Besides, the capital controls never bit as hard as expected: the government started to lift them almost immediately for foreign companies, and even for domestic ones they were never all that difficult to get round. They have now mostly gone.

But the peg remains. As Mrs Zeti puts it: “In the past couple of years, I've been told that the ringgit ought to be at 3 and at 4.5 to the dollar. Such wide swings are highly destabilising. We certainly have no difficulty in maintaining the peg: in the past year our reserves grew by $3.5 billion.”

Malaysia's total trade adds up to more than 200% of its GDP, so pegging its currency to the dollar, in which most of that trade is denominated, makes some sense. But some economists reckon that now might be a good time to come off the peg. Trade surpluses have been piling up for five consecutive years, and reserves are higher than they were before the 1998 devaluation. The market, though, plainly expects the peg to stay for a while yet.

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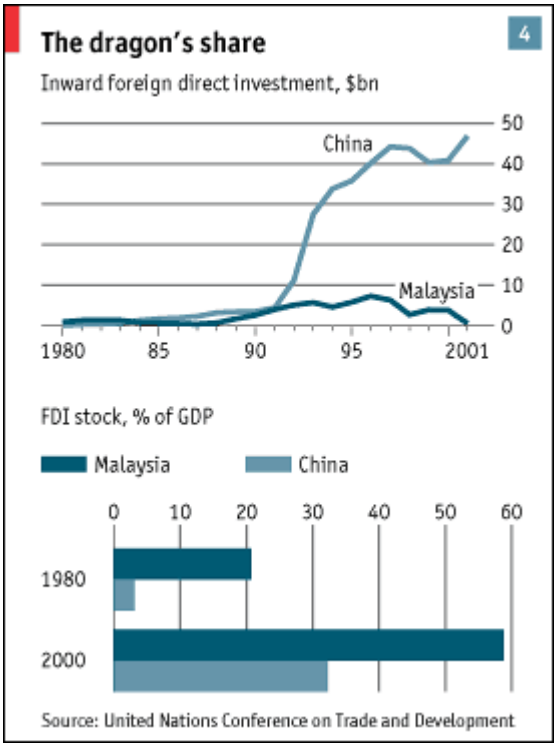
Keeping up with the neighbours

Apr 3rd 2003
From The Economist print edition

The country is rediscovering old skills and learning new ones

IT MUST have looked like a sure-fire winner. With a well-educated, English-speaking workforce and a relatively low cost base, Malaysia was favourably placed to take advantage of the wave of investment that rolled into South-East Asia in the 1980s and 90s. With the original four “little dragons” (Hong Kong, Singapore, Taiwan and South Korea) rapidly moving towards developed-country status and therefore becoming more expensive, the search was on for the next winners. During those two decades, some $80 billion was invested in Malaysia, turning it into one of the world's most export-dependent economies: only Singapore and Hong Kong, both tiny city-states, sell more abroad as a proportion of GDP. In the 30 years from 1970 to 2000, Malaysia's economic growth, despite the Asian crisis of 1997-98, averaged about 7%.

But the good times could not last. Malaysia's eggs were all in one corner of one compartment of one basket. Its economy was overwhelmingly based on foreign direct investment (FDI); the FDI was concentrated in the electronics sector; and the electronics sector, in turn, was highly dependent on selling (or, to be more precise, re-exporting finished products) to the American market. For all Dr Mahathir's ranting about Wall Street, the IMF and the iniquities of the global trading system, nowhere in the world except Singapore has done better out of trading with America.



China is a big part of the problem. For the past five years, it has been sucking in the dragon's share of Asian, not to mention global, FDI: its intake accelerated again after 1999, when it clinched the trade deal with America that two years later allowed it to join the WTO (see chart 4). In the mid-1990s Malaysia was pulling in $5 billion-7 billion a year in FDI: now the total is down to well under $1 billion. China, meanwhile, is heading for $50 billion a year. At the same time, Malaysia's markets have contracted. The slowdown in the American electronics sector has hit Malaysia particularly hard.

The problem can only get worse. Between 2005 and 2007, Malaysia will have to start complying with new regional and WTO trading rules that will throw its markets wide open to competition. The effect will be

particularly hard felt by Malaysia's domestic carmaker, Proton, which relies for its success at home on the huge import taxes payable on foreign cars. The opening of the markets, the government fears, is likely to push up unemployment, and drive voters into the hands of PAS.

Yet for all that, Malaysia's economy still looks remarkably robust. Last year the economy grew at an impressive 4.2%, more than Singapore (2.3%) or Hong Kong (under 2%). The reason: Malaysia has been admirably agile in reinventing itself. Under the British, Malaya was a highly successful commodity economy, its tin, rubber and palm oil helping to fill the colonialists' pockets far out of proportion to the country's size. Then it turned itself into a manufacturer. Now it is changing again.

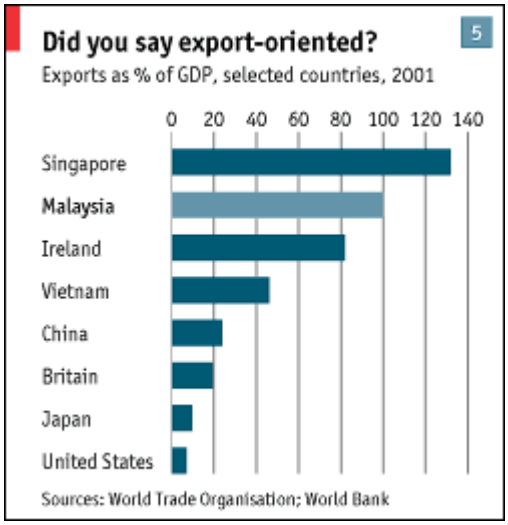
According to Noordin Sopiee, chairman of Malaysia's Institute of Strategic and International Studies and a close adviser to Dr Mahathir, the old economic structure never had as much going for it as generally reckoned. Intermediate imports account for 60-70% of the value of exports, he says, meaning that relatively little value is added in Malaysia. Allow for the fact that most of the firms generating those exports are foreign-owned and probably employ a number of foreign workers, and the benefit to Malaysia's economy is less than meets the eye. The dependence on manufacturing, he believes, has to be reduced.

As the realisation sinks in that the so-called “East Asian economic model” is doomed, a multiple strategy is emerging. One element of it is to boost domestic demand to make Malaysia less dependent on the global economic cycle. Another is to pay more attention to the traditional commodities that made Malaysia rich: palm oil, rubber and crude oil. Probably the most significant change is the new emphasis on services. But manufacturing still accounts for more than 30% of the economy, so Malaysia (like everyone else, unfortunately) is “climbing the value-chain”, trying to move its electronics industry up from commodity chipmaking to testing and even design, in the hope of staying a step or two ahead of China.

One advantage Malaysia enjoys is size. Unlike Singapore and Hong Kong, it has a large domestic market that can provide a cushion when times get tough. Gan Kim Khoon, executive director of AmResearch, part of the AmBank group, thinks this has helped the country keep its GDP growing by 4-5% a year or better, despite a depressed global trading environment. Infrastructure spending is a big part of it. With a high savings ratio and reserves of more than $33 billion (and rising), Malaysia has been able to finance a veritable orgy of building: roads, dams, the new airport and much else. It is true that the government has now run a budget deficit for each of the past six years, but government debt still amounts to an affordable 45% of GDP, especially as interest rates are among the lowest in Asia. On the external side, the debt-service ratio is a piffling 5%.

Still, much more could be done to boost the economy. The savings ratio may be high, but the investment ratio is notably low. Malaysian banks, still wary after the 1998 crash, are circumspect in their lending, and the demand for credit is anyway limited. Reformers such as Mohamed Ariff, who heads the Malaysian Institute of Economic Research, would like to see the government cut corporate and income taxes, which are high for Asia (though low by western standards) in order to stimulate demand. To stop the budget hole from getting bigger, he would be happy to see a cut in government spending, arguing that the infrastructure is now in pretty good shape.

Malaysia, unlike other little dragons, also enjoys a few stabilisers in the form of natural resources. Palm oil is proving especially handy just now: its market price is around 1,600 ringgit a tonne, more than double its level a few years ago. Some of the rise is due to increasing affluence in India and China, boosting demand for vegetable oils instead of animal ones. Malaysians are also improving revenues from their rubber trees by growing more cost-effective varieties. And Petronas, the state oil and gas company, has been turning in bumper results, largely thanks to higher oil prices but also, say foreign businessmen, to a greatly improved management team.



Service with a smile

Services look like a good bet. Tourism is the obvious one (see article), but Malaysia is also branching out in less expected directions. In health care, for instance, it is emerging as a cheaper alternative to Singapore or Hong Kong

for operations, nursing homes and the like, serving the affluent of the whole of East Asia. Cosmetic surgery is a speciality, particularly in Penang, the home of Malaysia's electronics industry, leading one wag to comment that Penang is advancing from silicon to silicone.

Tapping into a related market is the government's successful “Malaysia My Second Home” programme, aimed mainly at the retired. To get a long-stay visa, all they have to do is deposit 100,000 ringgit (150,000 ringgit for a couple) in a Malaysian bank. Education is another blooming sector. Since tertiary education was liberalised in the 1990s, both Melbourne's Monash and Britain's Nottingham universities have set up fully-fledged campuses in Kuala Lumpur, and there are scores of new Malaysian-owned universities and colleges. Increasingly, these are attracting the well-heeled from elsewhere in the region, because they charge much lower fees than western universities.

The big gamble, though, is on high-tech services. Dr Mahathir has pushed through the creation of a gigantic electronic business park called Cyberjaya, mid-way between the Petronas Towers and the new airport, and close to his gleaming new capital, Putrajaya. Geographically it makes good sense, since all the new creations use the same (toll) road and plug into the same fibre-optic spine. Cyberjaya lies at the heart of the much larger Multimedia Super Corridor (MSC), which runs from the towers to the airport. With a total area of 750 sq km (290 square miles), one MSC official proudly points out, it is about 100 sq km larger than the whole of Singapore.

The MSC is actually less a place and more a state of mind. Companies engaged in suitable high-tech services (the MSC is emphatically not for manufacturing) that set up within it are granted “MSC Status”, a lavish and coveted package of benefits that has now been handed to about 800 companies. Critics argue that these are conferring an unfair advantage on an area that is already one of the richest in the country, and that it would have made more sense to locate it near Penang, in the north, where Malaysia's (mainly hardware) electronics skills are concentrated. The government holds out the prospect of introducing similar schemes across the country in the future, but that will depend partly on the private sector, which built Cyberjaya.

The MSC is not attracting technology of a hugely advanced kind, but it is generating lots of jobs for all that. HSBC, a London-based bank, has chosen Cyberjaya as one of five worldwide back-office data-processing centres (alongside two in China and two in India). Ericsson, Fujitsu, DHL, Shell, Standard Chartered, Citibank, Nokia, Western Union, Hewlett-Packard, Intel and BMW are among the long list of companies that have regional data-processing or customer-service centres in Malaysia, mostly within the MSC.

Kent Yearsley, chief executive of Scicom, a five-year-old company that operates contract call centres, reckons that Malaysia, and the MSC in particular, offer unbeatable attractions. Labour costs are typically half the level in Singapore or Hong Kong, and land is even cheaper. The MSC pledges that the state-owned telecoms provider will match telecoms tariffs anywhere else in the region. It also offers zero corporate tax for a minimum of five years, generous R&D grants, and a guarantee that qualified expatriate staff will get working visas in a maximum of ten days. All of Scicom's 800 staff are at least bilingual in English and Malay, Mr Yearsley says, and many speak Mandarin and Cantonese as well. Scicom's call centres handle seven Asian languages plus English, and are about to add Japanese. To him, the benefits of Malaysia are obvious. Even Singapore Telecom seems to agree: it is setting up its own call centre in Melaka.

The MSC is even starting to attract software developers. Japan's giant NTT has its second-largest R&D centre outside Japan at Cyberjaya (the largest is at MIT) and is developing software and content for third-generation mobile phones there. At the other end of the scale, there is AccTrak21, a small software firm developing a range of accountancy software. AccTrak21's founder, Tim Loving, chose Malaysia even before the MSC got under way, having worked out that after allowing for all expenses (including labour, rent, utilities and taxes), the cost of developing software in Malaysia is about 5% of that in America.

It is too early to judge the MSC a success: most of the jobs created have been at the low end of the value-chain, and have come partly in response to tax breaks that will be expensive to continue indefinitely. But the signs are quite encouraging.

Poor Penang

Greater uncertainty surrounds the future of Malaysia's high-tech manufacturing industry, centred on the mainly Chinese island of

Penang. Penang took the lion's share of the FDI in the 1980s and 1990s, and has been the worst hit by the double blow of Chinese competition and weak American demand. The Penang Development Corporation's figures show that there has been no new “big lump” investment (over $100m) by multinationals in the island since mid-2000, though some smaller-scale investments have been made by firms that are already based there. Penang has managed to turn itself into a centre for testing and prototyping, but moving from there to research and design would mean a huge leap. “Forget it,” says one western management consultant. “It isn't going to happen.”

The gloom is almost palpable in the city, which these days looks grubby and unconfident. Many factories are now running only two eight-hour shifts a day, not three, and there have been lay-offs. Hotels such as the magnificently restored Eastern & Oriental are struggling to maintain 25% occupancy. The state government these days seems to be trying to sell Penang as anything but an electronics hub. It has become home to the World Fish Centre and boasts no fewer than five heart clinics, where a multiple bypass will cost you about a quarter of what it would in Singapore. The “Silicon Island of the East” label is being quietly sidelined.

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An effusive welcome

Apr 3rd 2003
From The Economist print edition

The more tourists, the merrier

THE foreign investors may have decamped for China, but the Chinese are coming to Malaysia—on holiday. That, at least, is part of the big plan for reinventing Malaysia as a service economy. Tourism already accounts for more than 5% of GDP, as in Thailand, and the government reckons it could go much higher. One target is the new rich in China, potentially hundreds of millions of them. Last year the number of Chinese tourists exceeded half a million, treble the 1998 figure.

The Middle East is another potential source of visitors. Since September 11th, Arab tourists have been reluctant to visit America and even Europe, and Malaysia has managed to cash in. Overall, though, the terrorist attacks on America have worked against Malaysia: Britain, America and Australia have all issued advisories against travel to Malaysia at various times. All the same, tourism revenues for 2002 were slightly up on 2001.

Abdul Kadir, Malaysia's enthusiastic tourism minister, reckons that his country has a bit of everything to offer. Kuala Lumpur shopping is probably second to none in Asia. As in better-known Singapore and Hong Kong, most foreign-branded luxury items are tax-free, and prices are keener because costs are lower. Household staples such as food and petrol are far cheaper, giving Singaporeans a big incentive to pop next door for their shopping. No surprise, then, that more than half the 13m tourists visiting Malaysia last year were Singaporeans, who stayed for an average of four days and spent a lot of money.

Shopping, though, is only a small part of it. Spacious and uncrowded, Malaysia can offer not just luxury beach resorts but vast national parks, some of the best diving in Asia and beautiful mountain scenery at Mount Kinabalu. It may lack the fleshly attractions of Thailand and the danger-laced exoticism of Indonesia, but it is a great place for a family holiday.

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A qualified success

Apr 3rd 2003
From The Economist print edition

On balance, Dr Mahathir has done well by Malaysia. But he should not linger

Reuters

It hurts to say goodbye

BY HIS own exacting standards, Dr Mahathir should probably be rated a failure. Barring a miracle, it is hard to see how the plans he outlined for Malaysia in a speech made in 1992, which became known as the “Vision 2020”, could possibly be realised. The main goal he set out was that by 2020 Malaysia should become a “fully developed country”, meaning that its income per head should get close to that of the 30 countries of the OECD. But last year the country's GDP per head was around $3,900, against an OECD average of $23,100, and the gap is widening.

The other targets in the “Vision 2020” are scarcely less ambitious, and equally unlikely to be accomplished. Malaysia has done well in fostering racial harmony in difficult circumstances, but in a land where discrimination remains legally embedded in most walks of life, a “united Malaysian nation” is still a long way off. A third great challenge, of “fostering a mature democratic society”, remains unmet too, as the treatment of Anwar Ibrahim and of the Keadilan opposition attests.

But it is unfair to judge Dr Mahathir by his own criteria. By less stringent ones, his rule has, on balance, been a time of success for Malaysia, especially when compared with neighbours such as Indonesia, the Philippines and Thailand, all of which have known worse government and weaker economic performance.

A larger canvas?

On October 23rd, days before he steps down, Dr Mahathir will welcome the other 55 members of the Organisation of the Islamic Conference (OIC) to Putrajaya for their triennial summit meeting. One task for the summit may be to choose the next secretary-general of the OIC in succession to Abdelouahed Belkeziz, who is likely to stand down at the end of next year. Dr Mahathir must be the leading candidate for the job if he wants it.

He would be a good choice. Dr Mahathir is the nearest thing on offer to a candidate who can bridge the chasm of misunderstanding between the Islamic and the western worlds. Although he has at times been famously critical of the West, his country, unlike most other OIC members, shares many western values. Malaysia is a democracy, if an imperfect one, which is true of only a very few Islamic countries. It is also tolerant of other religions, as many OIC members are not. It embodies a secular, modern Islam.

Most important, Malaysia is an economic success story, well integrated into the world trading system, and steadily increasing the living standards of its people. One of the principal sources of the new Christian-Muslim divide is the economic failure of most Islamic states, and the resentment of the West that this naturally if mistakenly breeds. Despite its government's heavy-handedness, Malaysia offers a good role model for the rest of the OIC.

Installing Dr Mahathir in Jeddah, where the OIC is based, would have another great advantage, for Malaysia at least: it would get him out of the country. The idea that he might install himself as a sort of honorary president-for-life, as Lee Kuan Yew has done in Singapore, is unappealing. His successor will need the freedom to make changes, such as loosening the over-cosy links between UMNO and business, easing the government's iron grip on the press and releasing people who are, in effect, political prisoners.

Even if he takes no formal title, Dr Mahathir is hardly likely to fade away. He has already tried to impose his choice of future deputy prime minister on his successor, though Mr Badawi has so far held firm. He has also said that he may remain an MP.

According to an old joke, the difference between Malaysia and Britain is that in Britain the prime minister is chosen every five years and the monarch rules for life; whereas in Malaysia the king changes every five years and the prime minister rules for life. There is some truth in that: since independence in 1957, Malaysia has had 12 kings (because the title rotates among Malaysia's sultans and rajas) but only four prime ministers. The greatest service Dr Mahathir could render Malaysia after all these years would be to retire, full stop.

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Apr 3rd 2003
From The Economist print edition

Besides those mentioned in the text, the author would like to thank the following for their time and their ideas:

Steven Gan, Malaysiakini; Tan Siok Choo, ISIS; Anual Bakri, chief minister's office, Kelantan; Ho Kay Tat, *The Edge*; Raja Aziz Addruse and Sankara Nair, lawyers to Anwar Ibrahim; Wan Azizah, Keadilan; Lim Kit Siang, DAP; Patrick Chalmers, Reuters; Garry Prior, Celadon Capital; Z.J. Cama and John Coverdale, HSBC; Brian Paul, Port of Tanjung Pelepas; Francis Yeoh, YTL Corporation; Khairy Jamaluddin and Ahmad Zaki Zahid, deputy prime minister's office; Abdul Azim Zabidi, National Savings Bank; Chandra Muzaffar, International Movement for a Just World; Tengku Razaleigh Hamzah, UMNO; Syed Azman, PAS; Zainah Anwar, Sisters in Islam; Edmund Gomez and K.S. Jomo, University of Malaysia; and Kean Wong, BBC.

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Apr 3rd 2003
From The Economist print edition

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The spoils of war

Cleaning up

Apr 3rd 2003 | NEW YORK
From The Economist print edition

Reuters

Who is winning the contracts to rebuild Iraq—and why?

Get article background

NO LONGER can opponents of the war in Iraq claim that it is “all about oil”. It is also now about digging roads, putting up bridges and building hospitals, schools and power plants. Even before America's soldiers set foot in Baghdad, its government has been dishing out contracts to rebuild Iraq. Stevedoring, a Seattle-based transport-services firm, has won a $4.8m contract to improve Iraq's only deep-water port, at Umm Qasr. International Resources Group, a professional-services firm based in Washington, DC, has a $7m contract to help set up a humanitarian-aid programme for Iraq. America's foreign-aid agency, USAID, has been collecting bids to build roads, train teachers, print textbooks, strengthen civic society—oh, and to build a universal health service in Iraq, too. USAID will not say how much it has to spend. But these first contracts may be worth $2 billion. Much more may follow.

As an agency which prides itself on its good works, USAID must be feeling a bit bruised. The eight contracts for “reconstruction activities in Iraq” which the agency made public recently have met with anger and stunned incomprehension. Appalled pundits splutter at the “grotesque” spectacle of American firms “profiteering” from the war even before the shooting stops. Workers at Bechtel, which is said to be leading the bidding for a $600m infrastructure contract, have had to wade through crowds of protesters chained to the doors of the firm's headquarters in San Francisco. Foreigners, somewhat confusingly, seem equally appalled that they have not been given the opportunity to profit from the war as well: only American firms have been allowed to bid. USAID's use of “secret” shortlists of bidders, meanwhile, has led much of the world's press to conclude that only cronies of President George Bush's inner circle need apply for the work.

Phony cronyism

In truth, the bidders are a broad church. A fuss over Halliburton, Vice-President Dick Cheney's old firm, has receded after the press reported that it failed, after all, to make the shortlist for the $600m infrastructure contract, apparently losing out to big engineering firms such as Bechtel and Fluor.

Stevedoring seems well-qualified to run the port at Umm Qasr. With offices from Bangladesh to Vietnam, it boasts that it “oversees more international operations than any other stevedore and terminal operator”. Charito Kruvant, president of Creative Associates International, a “minority, women-owned and managed firm”, based in Washington, DC, that is said to be USAID's preferred choice to revamp Iraq's education system does not sound like a typical conservative crony of Mr Cheney. She signs the firm's “message from our president” with “Peace, Charito”.

USAID officials are vague about the provenance of the agency's eight contracts, saying only that they were drawn up after “wide consultations” across government departments in January. Officials say that they used shortlists of bidders so that they could award contracts faster. Think-tanks such as the Centre for Strategic and International Studies (CSIS) have pressed the government to have its reconstruction plans for Iraq ready to go as soon as the shooting stops. From Haiti to Afghanistan, say the CSIS and others, past nation-building efforts have worked poorly in part because of the gap between ceasefire and the start of reconstruction. USAID's infrastructure contract talks about a post-war reconstruction effort as a “highly visual symbol of good faith towards building trust...as well as for political stability in the region”, a hearts-and-minds campaign which should be started quickly. Had it opened the contracts to full and transparent competition, says USAID, the process might have taken six months.

The shortlists were not made public, say USAID officials, because that is what federal procurement rules require to protect the “integrity of the bidding process”. The rules also say that American aid contracts must go to American firms, says USAID, so foreigners were not able to bid.

USAID did, however, waive nationality requirements for subcontractors, after Britain's Department of Trade and Industry kicked up a fuss. Up to 50% of the eight primary contracts can be farmed out to subcontractors, says USAID. Except for firms from countries on America's list of terrorist-sponsoring nations, say officials, firms of all other nationalities (yes, even the French) are welcome to apply. Crown Agents, a British development firm, has won a small contract. Costain, a British engineering firm, is in talks about another.

Costain has also landed itself in hot water, thanks to reported remarks by the firm's boss, Stuart Doughty, that putting the UN in charge of rebuilding Iraq would make the process slower and more inefficient. The UN points out that it rarely awards reconstruction contracts itself. In Afghanistan, Kosovo and elsewhere, contracts have been handed out, after donor conferences, by national government agencies (mainly to their own domestic firms, even in countries that claim to have “untied” their aid)—although the UN has often helped to administer reconstruction contracts on the ground. Even so, sources at the UN agree that Mr Doughty's comments (which he now denies making) are “obviously not illegitimate”.

What is clear is that the row over who governs post-war Iraq is hurting British and other foreign firms hoping to win some reconstruction work. Britain and France want the UN in charge, as it was in Kosovo and Afghanistan. The British government thus wants no association with any “long-term” contracts which might imply that the Americans plan to step in and run Iraq instead. In such circumstances, the government's lobbying efforts on behalf of British commercial interests have had to be unusually restrained.

A lot of the work on offer from USAID goes beyond aid, and appears to assume that America will involve itself closely in running Iraq for at least a year. The education contract, for instance, calls for the winning firm to promote “rapid school enrolment and sustained retention in the school system”, in part by building at least five “pilot projects in accelerated learning using politically neutral course content”. A contract to support local institutions asks the bidder to “strengthen local administrations, civic institutions and processes in Iraq”. As the CSIS said in a report after the publication of the USAID contracts, America appears to be preparing not just to deliver short-term aid to Iraq, but to implement a dazzlingly ambitious plan “on a par with American efforts in Germany and Japan” after the second world war.

America's apparent ambitions in Iraq are as controversial at home as they are abroad. USAID has spent much of the past week furiously backpedalling, insisting that its contracts are short-term and serve merely to “jump-start” Iraqi reconstruction. The American public is starting to worry about the cost—and nobody knows how exactly Iraqi oil money might be used to pay the bill. Whatever else this means, firms should probably not start totting up their spoils of war just yet.

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The effects of SARS

Business travaillers

Apr 3rd 2003
From The Economist print edition

Death, war and pestilence. What next for corporate travel?

IN AN almost biblical way, the riders of the apocalypse are descending on the travel industry. Death (the terrorist attacks on September 11th), war (with Iraq), and now pestilence (a killer pneumonia) are hitting airlines, hotels and conferences. SARS (Severe Acute Respiratory Syndrome) is hitting hardest in Asia, the last bastion of growth in the travel industry.

Hervé Gourio, president and chief executive of Carlson Wagonlit Travel, the world's second-biggest corporate travel-management firm, expects business-travel revenues in Asia—a fifth of a $250 billion global business—to fall by about 5% this year. That compares with double-digit growth in each of the past four years.

Reuters

The new fear of flying

The forecast may prove conservative. SARs, which has so far killed 78 people and infected some 2,200, is, says BNP Paribas Peregrine, an investment bank, a bigger threat to the region than the Iraq war and could “cast a long dry spell” over airlines, hotels and trade. That is worrying, given that business travel is already in a slump everywhere else. Even before the start of the war with Iraq, revenues from corporate travel this year were down by 5% in Europe and by 10% in America. The Iraqi conflict has probably lopped another 5% off, says Mr Gourio.

The reaction to SARs from companies, big and small, has been immediate and severe. Many (including *The Economist*) have advised staff against travelling to and from many parts of Asia. HSBC, the largest financial institution in Hong Kong, is putting plans in place for an emergency trading room. On April 2nd the World Health Organisation issued its first-ever travel alert, saying that infections had not yet peaked and that visitors should avoid Hong Kong and Guangdong province in southern China, where the disease is most virulent. America's State Department had earlier issued its own travel warning.

SARS and the war in Iraq have pushed some tottering airlines into deeper difficulty. On April 1st Air Canada, which has lots of routes into Asia, sought bankruptcy protection from its creditors. Several American airlines, including United, have already gone bust, though this week US Airways climbed out again. Congress has proposed yet another $3 billion rescue package to help to keep them airborne, though the administration is loth to sign on to more bail-outs.

The pneumonia outbreak is putting severe strains on Asia's once highly profitable carriers. Early estimates suggest that the number of passengers flying into Hong Kong has slumped by 30% in recent weeks. Cathay Pacific, Qantas and Singapore Airlines have all announced cuts in routes and mothballed airplanes. Peter Negline, an analyst at J.P. Morgan, estimates that a 10% drop in passenger traffic would cost Cathay Pacific HK$10m ($1.3m) in profits per day. Domestic airlines, such as China Southern and China Eastern, may suffer even more. The only good news is that Cathay's cargo business is holding up as technology companies build up their inventories, just in case there is a disruption to the airfreight business later.

Things look at least as bad for the global hotels and conference markets. The World Economic Forum said on April 1st that it was delaying a big meeting on Chinese business in Beijing. General Motors is postponing a conference it was to have held in Shanghai, and Intel said on April 2nd that it would cancel technology events in Beijing and Taipei. Bookings for hotels in Hong Kong are down by about 30% on a

year ago, and by 20% in Singapore. Some hotels in Singapore are seeing occupancy rates fall below 30%.

Despite the gloom, some analysts reckon that the public is overreacting to the threat of SARS—after all, 36,000 people a year die of flu in America alone. They believe that there is a big pent-up demand for travel, and that the business market will rebound. Firms are switching to cheaper ways to communicate, from video-conferencing to e-mail. But such technologies are still inferior to face-to-face meetings. Until they improve, it will take more than SARS to kill off business travel.

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Theme-parks in Japan

Welcome to bankruptcyland

Apr 3rd 2003 | TOKYO
From The Economist print edition

Disney may be prospering, but many theme-parks in Japan are going bust

ON APRIL 15th, Tokyo Disneyland will celebrate the theme-park's 20th birthday. It has plenty to cheer. Oriental Land, Tokyo Disneyland's local parent, made back its initial investment of ¥180 billion ($1.5 billion) in just four years. Since then it has invested in fresh attractions, opening Tokyo DisneySea, a sister park with an ocean theme, in 2001. Oriental Land says its parks had 25m visitors in the year to March 31st, 13% up on the year before.

Even more remarkably in recession-hit Japan, Oriental Land's net profits are expected to rise by almost 40%, to a record ¥17.7 billion. Such is Tokyo Disneyland's popularity that the son of North Korea's dictator, Kim Jong Il, was reportedly caught sneaking into the country to visit the magic kingdom a couple of years ago.

EPA

Going downhill fast

Yet Tokyo Disneyland stands out in an industry struggling to survive. Its success spurred a theme-park construction spree during the bubble years. Many parks had international motifs: there are at least three New Zealand “villages”—with lots of sheep—as well as German, Swiss, Turkish, Spanish and Russian theme-parks. Many were badly-planned joint ventures between local governments and private firms, encouraged by new laws in the 1980s that provided loan-guarantees, tax breaks and low interest rates.

Nagasaki, on the southern island of Kyushu, sponsored two Dutch theme-parks. The smaller one went bust last June. The other, Huis Ten Bosch, collapsed in February with liabilities of ¥229 billion. The most spectacular bust took place in 2001, when Seagaia, an 850-acre resort which boasted the Ocean Dome, the world's largest waterpark, collapsed with liabilities of ¥276 billion. Having cost local governments and Dai-ichi Kangyo Bank ¥200 billion to build, it was sold to Ripplewood, an American private-equity fund, for under 10% of its construction costs.

Unlike Tokyo Disneyland, sitting in the most heavily populated area in Japan, many theme-parks are relatively isolated. Seagaia's hotels had more rooms than there were seats on flights into Miyazaki. But the concept is crucial too. Navel Land, a theme park in Fukuoka, is so named because it is supposedly located where the “bellybutton” of the island it is on would be. But perhaps visitors have stayed away because of its theme: coalmining.

Others have suffered because of the ballooning problems of their financiers. Gulliver's Kingdom, located at the foot of Mount Fuji, complete with a 45-metre statue of the character from Jonathan Swift's novel, was forced to close down in 2001 after its biggest creditor, Niigata Chuo Bank, went bust.

Satoru Shinozuka, of Teikoku Databank, a research firm, reckons that three-quarters of Japan's theme-parks are now struggling. This may now include Universal Studios Japan, part of Vivendi Universal, a troubled media group, which opened in 2001. The theme-park has suffered a sharp decline in visitors recently after a series of scandals, which included falsifying labels and serving beef and salami that was past its sell-by date, and failing to report that one of its drinking fountains had been pumping out untreated industrial water for nine months.

The outlook is not encouraging. Japan Travel Bureau (JTB), the biggest travel agency, reckons that the

number of domestic travellers will drop a bit this year, partly because several public holidays fall on awkward days. Worse, some analysts fret that banks, now facing “special inspections” into their non-performing loans by the regulator, may soon cut off funding to many dud projects, though it remains to be seen whether they really will.

Yet some operators are fighting back. A recent trend has been to create *onsen* (hot springs) theme-parks in urban areas. Three are opening in Tokyo this year. These hope to cash in on the Japanese love for public baths, and to expand their customer base to include families, elderly folk and young women on their way home from work. For many parks, the city of Yokohama, which bought Yokohama Dreamland after it closed last year, may have the most fitting solution: it plans to turn it into the ultimate dreamland, a graveyard.

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Tobacco lawsuits

Going up in smoke

Apr 3rd 2003 | NEW YORK
From The Economist print edition

A golden goose faces slaughter

MUCH was inevitable about the massive $12 billion judgment given against Philip Morris in late March by a judge in Madison County, Illinois. The case was about misleading adverts that had downplayed the hazards of cigarettes marketed as “light”. But had this claim failed another would have followed. Madison County, along with Jefferson County, Mississippi, and the state of West Virginia, has become an open vault for trial lawyers pursuing legally vulnerable rich companies. Altria, the parent of Philip Morris, is the fourth most-profitable firm in America, with legal exposures unlikely to disappear until the company is dead.

Philip Morris was bound to respond to the huge verdict by appealing and doing all in its power to resist posting a required $12 billion bond. This has included pushing for new legislation in Illinois and urging states expecting money from a prior legal settlement to weigh in on its side to protect their winnings. It is one of the ironies of the Philip Morris case that successful litigants have a greater interest than most in the tobacco giant thriving, which will require all the usual ingredients that allow firms to prosper, including cheap financing, the best modern marketing—and success in later lawsuits.

Since the verdict, Altria's shares have dropped by 20%. Its bonds have also tumbled as the rating agencies have downgraded the firm's credit to borderline junk. This will raise financing costs and depress profits, which is not in the interest of any claimant and is particularly harmful to the states which had been first in line for the firm's money. This highlights a big cost in using lawsuits to resolve such matters. Because of the nature of litigation, in each case only the interests of the litigating parties are considered and not the broader interests of society, notes Judyth Pendell, a senior fellow at the AEI-Brookings Joint Centre, a think-tank.

Perhaps the government could intervene to balance the claims of different interested parties. Another possibility is for Altria to enter Chapter 11 bankruptcy, allowing a judge to sort out the mess. The firm says it is adamantly opposed to this approach, which would be rejected both by the states and by investors who have bought bonds backed by tobacco-settlement money issued by states. But given the firm's seemingly infinite legal exposures, it may be inevitable.

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Mobile telecoms

No text please, we're American

Apr 3rd 2003 | SAN FRANCISCO
From The Economist print edition

Text messaging is popular in Europe and Asia, but not in America. Why?

SAMUEL MORSE would be proud. The form of communication he pioneered, the telegram, may have gone the way of the horse-drawn carriage, but it lives on through that most modern means of keeping in touch: the text message. Every day more than a billion messages are zapped from one mobile phone to another. Like telegrams, the length of messages is strictly limited. Some phones even announce the arrival of a new message with three short beeps, two long ones, and three short ones—Morse code for SMS, the name of the most widely used form of text messaging.

But although texting has become commonplace in Europe and Asia, it has failed to take off in Morse's homeland, America (see chart). Globally, the average number of messages sent or received each month by a mobile subscriber is now around 30, or one message per day. Each message costs an average of $0.10 to send. In some parts of Asia, such as Singapore and the Philippines, where large numbers of free messages are thrown in with monthly pricing plans, the number of messages sent per subscriber per month is as high as 200. But the figure for America is just over seven, according to the Cellular Telecommunications Internet Association, an industry body. Why is such a high-tech nation eschewing texting?

The short answer is that, in America, talk is cheap. Because local calls on land lines are usually free, wireless operators have to offer big “bundles” of minutes—up to 5,000 minutes per month—as part of their monthly pricing plans to persuade subscribers to use mobile phones instead. Texting first took off in other parts of the world among cost-conscious teenagers who found that it was cheaper to text than to call, notes Jessica Sandin, an analyst at Baskerville. But in America, you might as well make a voice call.

Free local calls also make logging on to the internet, for hours at a time, and using PC-to-PC “instant messaging” (IM) the preferred mode of electronic chat among American teenagers. Although IM users are shackled to their computers, IM has the advantage over mobile texting that each message is free.

American telecoms regulations—which encouraged different mobile operators to choose different, incompatible technologies—are also responsible for the dearth of texting. Only last year did the largest American operators agree to pass text messages between their networks—an agreement still only patchily implemented. In addition, not all handsets sold in America support two-way texting: many older models allow only incoming messages. And texting is not included as standard in most subscription packages, but as an extra for which customers must pay a few dollars per month. “You have to pay for it, most people's phones don't have it, and I don't know how many of my friends have it enabled,” says Vince Tobkin, an analyst at Bain & Company in San Francisco. In text-crazed Europe, in contrast, where regulators have imposed a single mobile-phone standard, all these conditions are met by default and you can be pretty sure that your message will get through.

Admittedly, things have improved since the middle of 2001, when American mobile subscribers sent an average of just 0.3 messages per month. But since a surge at the start of last year, which was widely expected to carry texting into the mainstream, the volume of messages seems to have levelled off. Still, American operators are continuing to push texting through tie-ins with reality-TV shows and sporting

events, in the hope of boosting revenue and profits (margins on text messages are higher than on voice calls). They enviously eye Europe, where messaging accounts for 20% of some operators' revenues.

America is not wholly alone in its disdain for texting, however. There is one place in Europe that, on this matter at least, stands shoulder to shoulder with America. That country is France.

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Biotechnology

Show me the money

Apr 3rd 2003
From The Economist print edition

A takeover battle with a twist

BRITAIN is the source of what little life remains in the comatose world of mergers and acquisitions. The multi-billion-pound bid battle for Safeway, a supermarket chain, rumbles entertainingly on and is now mirrored, on a smaller scale, in the fight for Oxford GlycoSciences (OGS), a British biotech firm.

This week two new potential bidders entered the fray already started by two rival biotech firms—Cambridge Antibody Technology (CAT) and Celltech. They are a couple of British venture capitalists, Sir Christopher Evans (often regarded as the Richard Branson of British biotech) and Alan Goodman, who hope to buy OGS and parcel out its technology to other firms in their portfolio. Meanwhile, OGS says it has been approached by other potential buyers, including a big drug firm (rumours suggest AstraZeneca) and an American biotechnology company (maybe Medarex).

Bidding wars are scarce in the rarefied world of biotech. So why, with roughly 1,800 biotech firms in Europe and a similar number in America, are so many bidders chasing just one firm?

“Cash is the main driver here,” says Glenn Crocker, a consultant with Ernst & Young. OGS has roughly £130m ($205m) of cash, raised in the heady days of 2000, before the bubble burst. That exceeds its current market capitalisation of £108m. So much for the one product the firm already has on the market in Europe (for a rare affliction called Gaucher disease), as well as for an interesting library of drug targets generated by its proteomics division, which the market apparently values at less than nothing.

OGS is not the only firm whose cash exceeds its market value. Martyn Postle of Cambridge Healthcare and Biotech, a consultancy, points to several British firms, such as PPL Therapeutics and Pharmagene, now worth less than their cash reserves. Several American firms, such as CuraGen and Incyte Genomics, are in a similar position.

General economic gloom, combined with today's investor scepticism about the likelihood of biotech firms delivering profitable products, has dragged the sector down. Given past trends, biotech will soon be back in fashion again, with investors throwing money at it. But for now, investors seem interested in buying such firms as OGS more to take money out than to put more in.

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Anti-Americanism and television

The one where Pooh goes to Sweden

Apr 3rd 2003
From The Economist print edition

Do American television channels spread cultural imperialism?

WHEN the British government introduced a bill last year to make it possible for ITV, the country's top commercial broadcaster, to come under American ownership, it did not imagine that the bill would be going through the House of Lords at a time of such intense anti-American sentiment. Led by Lord Puttnam, the producer of such films as “Chariots of Fire” and a former production head at Columbia Pictures in Hollywood, a rebellion is brewing. As well as fearing the prospect of any more media power being given to Rupert Murdoch, a possible buyer of Channel Five, another commercial British channel, Lord Puttnam has repeatedly argued that American ownership would result in a (further) flood of imported American programming on to British TV screens.

At the same time, war has given a new lease of life elsewhere in Europe to old worries about American ownership spreading cultural imperialism. Only last week, President Jacques Chirac urged French TV to set up a 24-hour TV news channel, in response to fears about the growing influence of American-owned networks such as Mr Murdoch's Fox News and AOL Time Warner's CNN.

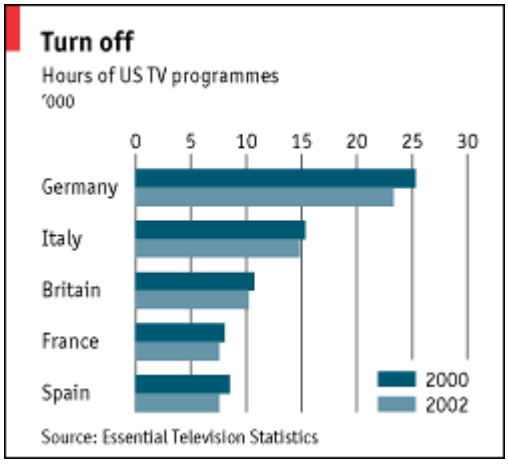
There may be reasons to worry. The logic of vertical integration—owning both content and distribution—rests on the ability to spread the cost of television programming across as wide an audience as possible. “The big American players,” argued Mark Fishlock of the Creators' Rights Alliance, an industry body, recently, “have shelves of programmes, already made and essentially paid for...which can neatly and cheaply plug many a gap in British TV schedules.”

Even so, such fears can be easily overdone. Yes, familiar American imports, such as “Friends” or “The Simpsons”, appear in prime-time. But most other American programming neither airs in prime-time, nor attracts huge ratings.

The critics may love such series as Fox's “24” or Warner Brothers' “The West Wing”, but British broadcasters shove them into late-night slots precisely because so few viewers tune in. The days when “Dallas” or “Kojak” filled British prime-time are long gone. Today, the top 50 British TV shows are all home-grown, led by the local soap-opera staples, “Coronation Street” and “EastEnders”.

Britain is no exception. Between 1996 and 2002, the number of hours of American programming fell by 26% in Spain, 17% in Germany and 9% in Italy, according to Essential Television Statistics, a research group. Since 2000, the drop has been marked in all five big European countries.

Quotas alone do not explain this trend. The European Commission recently reported that broadcasters in every European Union country are now far above the minimum 40% quota for EU-made programmes, devoting on average 62% of airtime to them. The top series in France in 2002 was “Fabio Montale”, a French cop series; in Spain, it is “Ana y los 7”, a Spanish soap. In short, consumers want local.



But what if an American company owns the distribution channel? Surely the logic of vertical integration is to force-feed already-made stuff down the tubes? In Europe, the only examples are pay-TV channels, such as Disney, MTV, or CNN. Yet, in each case, the most successful strategy has been, in the words of Chris Cramer, head of CNN International, to “de-Americanise” content. In 1996, 70% of programming on CNN International was American; by

2001, this had dropped to about 8%.

I want my local MTV

It was Viacom's MTV that pioneered this model. The company had originally thought that, because pop music is a genuinely global product, a single channel would prosper everywhere. But it soon learned that success depended on creating local versions of the channel. Since 2001, it has launched 14 new MTV channels, most recently MTV Romania and MTV Indonesia, bringing the global total to 38. Each is tailored to local tastes, literally: a top show on MTV Italy is “MTV Kitchen”, where musicians show off their favourite recipes. In Indonesia, MTV broadcasts a “funky but respectful” call to prayer five times a day. Sensitive to the damage that its link with America could do to its brand, MTV constantly tests its image. “We don't even call it an adaptation of American content: it's local content creation,” says one MTV executive. “The American thing is irrelevant.”

For all the fears about Mr Murdoch trampling over British TV, he too has become a disciple of localisation. When he bought StarTV in 1993, the plan was to use his Fox films and TV programmes to fill a pan-Asian channel. But it was not until Star hired local producers to make soaps, comedies and game shows for customised channels, in languages from Hindi to Mandarin, that the business began to prosper.

Even Disney, icon of Americana, has adopted a similar strategy. It recently launched a local version of the Disney Channel in Scandinavia, mixing familiar Disney characters, such as *Nalle Puh* (Winnie-the-Pooh), with local favourites, such as Pippi Longstocking. In Britain, over half of the output on Playhouse Disney is now British-made. A British studio makes for Disney a children's art series in various languages—in the best BBC tradition, complete with ample supplies of sticky-backed plastic and squeezy bottles—which is then broadcast to children in such countries as Mexico, Germany and France.

The key to this approach is to get the economics right, so that the extra cost of local production is commercially viable. Boosting locally raised revenues is critical. The more established a channel becomes, and the wider the audience it attracts, the greater the advertising base and the bigger the pot that can be devoted to local production. Ad revenues at MTV Europe, for instance, leapt by 32% in 2002 compared with 2001; as a result, MTV in Britain has doubled its programming budget for 2003.

Plainly, this strategy has limits. Consumers may be less satisfied with local versions of American-owned news, for example, than with kids' programmes. Hence Mr Chirac's push for a 24-hour news channel, just as CNN is said to be considering the launch of a French-language CNN.

For now, though, the moguls are making reassuring noises. As Viacom's Sumner Redstone, who has not denied being interested in Britain's ITV, put it recently: “In our programming, we have always been very attuned to local tastes. The idea that we would dump US programmes is absurd.” Even so, it appears that politicians do not trust Americans not to pump their own stuff down European tubes, and are putting other obstacles in their way. The British government is stepping up regulation of content even as it frees up ownership. Politicians, it seems, find it as hard to trust their own couch potatoes to watch what they deem suitable as they do to trust Americans to show it.

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Face value

It's not easy being French

Apr 3rd 2003
From The Economist print edition

EPA

Thierry Desmarest may have much to lose from his country's opposition to war with Iraq

WHO will get their hands on Iraq's oil? This may seem an uncomfortable, even tasteless, inquiry to make when the guns are still blazing—but there is no escaping the fact that it is one of the bigger questions lurking when the war is over. Critics of the war have accused gas-guzzling America of being motivated largely by the prospect of grabbing the world's second-biggest proven reserves of oil. Some Americans and British have been equally quick to blame French and Russian opposition to the war on contracts their oil firms have signed with Iraq.

Certainly, until the war started, one of the firms that seemed most likely to get its hands on Iraqi oil was France's biggest company, TotalFinaElf. Unlike its American and British rivals, such as Exxon Mobil and BP, which in recent years have had to stay away thanks to the hostility of their governments toward Saddam Hussein and their enthusiasm for United Nations sanctions, Total has followed the French government's lead and kept up contacts in Iraq. That seemed to pay dividends when it was reported that the company had secured lucrative deals to exploit the huge Majnoon field, with 20 billion barrels of oil, in southern Iraq, as well as the smaller Nahr Umr field nearby.

The war in Iraq, and the French government's energetic opposition to it, now threatens to dash the cup of victory from Total's lips. It seems far from likely that the Americans and British, who by dint of their troops are likely to have *de facto* control of Iraq's oil reserves for some time, will want to reward firms from countries that opposed their efforts to overthrow the regime of Saddam Hussein.

Some French businessmen see signs of what lies ahead in this week's reports that a blacklist is being prepared by the Pentagon on energy companies doing business in Iran—including Total, which in 1995 won the first big oil contract signed by the ayatollahs as American sanctions kept away their Texan rivals. Another sign of the current anti-French mood in America was a recent column in the *Wall Street Journal* that struck a relatively charitable tone when it argued that American "policy ought to be that all companies will have equal rights to bid for Iraqi oil deals when the fight is over—but only when [Jacques] Chirac and the likes of Thierry Desmarest, head of TotalFinaElf, are also gone along with the outlaw Iraqi regime they abetted." Ouch.

It may be unfair to make no distinction between the French government's opposition to war and abetting Saddam's regime, but what of the fairness of mentioning President Chirac and Mr Desmarest in the same breath? The French government has no stake in Total, but the company is still a "national champion" in

the classic French manner. It is deeply cosy with the government—although, let it be acknowledged, the firm that Mr Desmarest created in 1999 by a (controversially) hostile acquisition of Elf by Total is no hotbed of political corruption of the sort being revealed in the trial of former Elf executives and others now embarrassing France's political and business elite.

Some French businessmen have tried to distance themselves from their government, to curry favour with American customers. But only the other week, Mr Desmarest was happy to coo that the government's line on Iraq seems to him “a wise policy”. Soon after, Francis Mer, France's finance minister, returned the favour, by declaring that “there is no reason why European oil companies, notably Total, can't take part” in post-war Iraqi contracts. Last month, when Mr Chirac visited Algeria, he was cheered by 500,000 adoring locals for his anti-war stance. It was no coincidence that Mr Desmarest was there too, basking in reflected glory and unveiling plans to invest over $1 billion in Algerian gas projects.

Not so bad

Even so, there are reasons why even hawkish Americans should write off neither Mr Desmarest nor his company. For one thing, he may not be guilty of doing deals with Saddam. He says the reports of contracts signed with Iraq for Majnoon or Nahr Umr, or any other fields, are false. Yes, Total has talked for years with Iraq about these contracts—but whereas Russian and Chinese firms signed contracts, Total did not, because it respected international sanctions. Not that signing in itself would have breached the sanctions. But Iraq could have used the contracts to demand that Total begin work that would have done so.

There has in any case been speculation that firms which have signed contracts with Saddam will challenge American attempts to tear them up in the courts—potentially delaying for years the extraction of Iraqi oil and thus the generation of revenues needed to finance the country's reconstruction. Mr Desmarest says that Total would not participate in such legal actions as it has signed no contracts and thus has “no claims in Iraq”. If that does not completely exonerate Total in American eyes—after all, it has done everything but sign contracts, and still has an incentive to lobby the French government to oppose the war and get sanctions lifted—perhaps it should earn it a suspended sentence.

The other thing in Mr Desmarest's favour is that he is one of the best managers in the oil business. Indeed, his style is downright un-French, owing much to the best of American management. Some industry analysts think his attitude to oil, if not his accent, would not be out of place in Texas. He stresses shareholder value and capital discipline. Total's oil and gas output grew by 10% last year; its fourth-quarter profits were 13% up on a year earlier. Its return on capital beats even Exxon's. Even were it to miss out in Iraq, its prospects would be excellent. That may be why one-third of the firm's shareholders are American or British, and the dollar value of Total's American Depositary Receipts in New York has risen even in recent months. Perhaps that will continue. After all, Americans have only recently discovered Francophobia. Their love of a good investment is much older.

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Economist.com BUSINESS
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Wincott award

Apr 3rd 2003
From The Economist print edition

The Economist has won Britain's Wincott award for Business and Finance Journal of the Year in 2002. The judges particularly commended our coverage of America's corporate and financial wrongdoings (see our collection of articles on corporate misbehaviour).

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Business in bad times

Rising above the sludge

Apr 3rd 2003 | LONDON, MUNICH AND TOKYO
From The Economist print edition

As business conditions get tougher, which companies are best placed to thrive?

WHAT better places to turn for lessons in how to prosper in adverse conditions than Japan and Germany? The first has been hit by bouts of recession ever since its asset-price bubble burst in 1990, while sclerotic Germany has been hobbled by the EU's tough fiscal-policy regime, by rigid labour laws, and by the cost of integrating the former East Germany. The country has also been in and out of recession for the past three years.

For some months now, companies have been battening down the hatches everywhere, curtailing investment, slashing costs and reining back marketing. Some—the big car companies, for example—are slashing prices in a desperate effort to sustain sales and hold on to market share. Many middle managers in America and Europe have known only good times. Now that their markets are slumping, they are confused about how to react.

Companies that have flourished in recent years in the unpromising soils of Germany and Japan have, for the most part, followed a few key rules. Keeping your eye on the finances is never a bad idea: Kao, a thriving Japanese consumer-goods manufacturer that has almost turned cost-cutting into a religion, is expecting to be rewarded with its 20th consecutive year of record pre-tax profits.

Siemens, one of the world's biggest engineering groups, employs 430,000 people. Where competitors such as Alstom and ABB have struggled to weather tough economic conditions, the German giant has marched on, making handsome profits and increasing its share of its main markets. During the bubble of the late 1990s, it resisted the temptation to win business by offering financing deals to customers. Rivals that were less disciplined have subsequently had big problems, especially with debt-laden clients in the telecoms industry. Siemens was also diligent in avoiding disasters from loosely written contracts—disasters that have befallen some of its competitors.

As always, good management also makes a difference. Canon's successful assault on the American photocopier market has been orchestrated by the almost legendary Fujio Mitarai. After a spell running Canon's North American division, Mr Mitarai returned to Tokyo and welded the best of American business practices on to an oriental culture. Unlike Japanese companies such as Sony, however, Canon has remained deeply sceptical of Anglo-Saxon models of corporate governance. It does not, for instance, have outside directors.

The global card

Financial prudence and inspired leadership are good for all times. So what have successful companies in Germany and Japan done that has specifically helped them to rise out of the trough of recession?

One thing many have done is to go global. Globalisation is a natural counter-cyclical business strategy. When things are bad in a company's home market, they are sure to be less bad in other markets elsewhere. “The lesson of the past seven to eight years is that, if countries are deflating, companies need to go abroad and access demand elsewhere,” says Alexander Kinmont, an equity strategist at Nikko Salomon Smith Barney in Tokyo.

Toyota and Honda, the top two Japanese car companies, will report record profits for the year to the end of March. A large percentage of these are made in America. Today, around three-quarters of the cars that the two firms currently sell in America are also manufactured there.

Nissan, Japan's third big car company, was late in going global. When Carlos Ghosn moved in to rescue it, after Renault had bought a stake in 1999, he was struck by the way that Nissan's managers were full of excuses for the company's poor performance. They each blamed one another, and they all blamed the collapse of growth in the Japanese economy throughout the 1990s. But that was hogwash. In reality, Nissan's share of its home market had been eaten away by its two domestic rivals, Toyota and Honda. The belated build-up of Nissan's position in America has been a big factor in its recovery over the past three years.

Successful Japanese companies in other industries have also grown by going global. Last year's dramatic recovery by Sony was fuelled by sales of its PlayStation 2 console in America, and some 70% of Canon's revenues come from markets outside Japan. Ricoh, its rival in the copier-and-printer industry, derives half its sales—and half its operating profits—from overseas markets. Canon delivered its third year of record profits in 2002, and Ricoh is soon to report its ninth consecutive record year.

So successful have the two of them been that they have both overtaken Xerox, the undisputed market leader ten years ago, in several key parts of the office-equipment market in the United States. While Xerox's home market was booming, the American icon was caught napping by two foreigners whose home market was far from booming. Xerox disguised the full extent of its failure for a while by prematurely booking some $6.4 billion of revenues (and overstating its profits by $1.4 billion) between 1997 and 2001.

Takeda Chemicals, Japan's largest drug company, has been profitable for ten years in a row. It too earns a chunk of its revenues from overseas markets. This is particularly unusual because the domestic Japanese drug industry consists largely of smallish arms of big chemicals conglomerates, a business model that faded elsewhere in the world years ago. Takeda's success overseas has relied on some clever technology and on its marketing alliances with such global leaders as Eli Lilly.

German lessons

One of the most striking examples of a company thriving despite weaknesses and rigidities in its home economy is Germany's Volkswagen. With the state of Lower Saxony owning a fifth of its shares, VW could not react to the weak car market in the mid-1990s by slashing jobs. That would have been deeply unpopular with the local government, grappling then (as now) with high unemployment.

Forbidden to apply the brakes, VW slammed hard on the accelerator, launching new models (all based on a small number of chassis and engines) and ramping up production. It re-established its lead in the European mass market and enjoyed a revival in America with the new Beetle model that it launched in 1998 and that it manufactures in Mexico.

The other big German car companies have also played the global card well. Daimler-Benz took over Chrysler—to gain economies of scale and deeper access to the American market—and, after a shaky start, that deal now seems to be paying off. Likewise, BMW emerged from its botched purchase of Rover in Britain with the consolation prize of the British company's Mini brand, which has helped lift BMW's production volume up to a million.

Buying Chrysler meant that Daimler-Benz made a spectacular U-turn. The company had previously tried to diversify by turning itself into a conglomerate involved in all forms of transport. Jürgen Schrempp, its boss since 1995, opted instead to return to its core car business, but to be more global. Many of the non-car businesses were sold or closed down, although there are some leftovers, such as DaimlerChrysler's stake in EADS, Europe's biggest aerospace company.

Deep in the heart of Germany's famous *Mittelstand* of medium-sized companies there are many less-well-known cases of German enterprise surviving a sclerotic home economy. One example is Knorr-Bremse, a Munich-based manufacturer of braking systems for trains and lorries. Since a management buy-out in 1985, the company has grown steadily away from its German roots and now has 70% of its 11,000 staff abroad. As Heinz Hermann Thiele, its boss and owner, observes: “When I bought the company, sales were *euro*200m and the balance sheet was very weak. So I had to find a new strategy and reshape the business.”

He decided to focus on braking systems, then a part of the company with good potential. The market for the systems was fragmented, but the main customers—big engineering groups and makers of commercial vehicles—were increasingly global. So Knorr-Bremse set about becoming a global supplier.

It has integrated no fewer than 28 acquisitions since 1985, and its latest big deal (in early 2002) has made it the market leader in lorry brakes in America. (It also proved that recession need not be a bar to opportunistic takeovers.) Knorr-Bremse now commands 40% of the world market for braking systems used on trains and lorries. Last year's turnover of *euro*2.1 billion was three times that of 1996. “We are now a global company,” says Mr Thiele.

Sliced to the core

Diversification indulged in during good times often turns sour at the first sign of trouble. Telecoms and energy firms such as WorldCom and Enron were so keen to be more than boring service providers that they borrowed heavily in an effort to re-shape themselves into sexier businesses. The same was true of Vivendi, a dull but profitable French utilities group that floundered after a reckless bout of expansion and diversification, notably into American media. Marconi in Britain is another miserable example of a sound, if dull, company (the former GEC) which renamed itself as it diversified disastrously into high-tech telecoms companies just before the technology bubble burst.

Ford too strayed almost disastrously far from its core. Jacques Nasser, its former boss, was determined to turn the company into a provider of consumer goods and services related to transport. He embarked on a borrowing orgy as Ford bought companies—such as the Kwik-Fit car-repair chain—and launched itself into e-commerce. Top management was distracted from the basic business of carmaking. Product planning, quality control and capacity utilisation all developed problems; Ford went from making the biggest profits in the industry to struggling for survival in the space of less than three years.

In Germany and Japan, those companies that have stuck to their core business, and done it well, have generally thrived. Toyota and Honda are (and have been for a long time) simply very good at making cars that are attractive and appealing to consumers.

In Germany in the 1990s, Siemens successfully trimmed its broad portfolio of businesses, in particular spinning off its chipmaking arm in April 1999. It thought, correctly, that the chip business was too cyclical and too capital-intensive for it to make sense as part of a large engineering group. The spun-off business, now called Infineon, has done well on its own. As a standalone company, it has invested in impressive new production facilities at plants in Dresden and Regensburg.

By specialising in high-value chips, rather than commodity chips, and by focusing on designing chips for specific industries, Infineon has largely avoided the brutal competition from Asian producers that has wiped out much of Europe's chipmaking capacity. (A similar strategy has protected ST Microelectronics, a competitor.) It has not avoided the general troubles of its industry—in 2002 it lost money for the second year running—but it has loads of cash and has coped better than most.

Other thriving companies have focused on core disciplines, according to Kaoru Kobayashi, a professor in global management at the SANNO Institute of Management in Japan. Canon's pet passion is monitoring its cashflow. It is also sharply focused on extracting profits from economies of scale, says Steven Myers, an analyst at HSBC Securities. Thus many of its new components for image-processing are used in most of its cameras.

This is not to say that tightly focused companies cannot be innovative. But new products do not usually stray far from their core expertise. Kao has been extremely successful at developing hit products that fit within its range. Econa, a special low-fat cooking oil has enjoyed double-digit sales growth in Japan since its launch in 1999, despite being triple the price of normal cooking oils. Kao is hoping to take Econa to America and is now testing the product in Atlanta and Chicago. Another winning feature at Kao, says Ritsuko Tsunoda, an analyst with Merrill Lynch Japan Securities, is its knack of coming up with products that do not cannibalise its existing product line—crucial if the company is not to diversify too far from its core.

Nearly a third of Kao's headquarters staff now work on product development. Similarly, Canon ploughs nearly 8% of its revenues into research and development to protect and improve the core technologies that give it an edge over its rivals. Infineon too invests heavily in R&D, employing 5,400 people in the area out of a total staff of 30,000. Last year the company spent more than *euro*1 billion ($940m) on R&D, equivalent to 20% of its revenues.

Processes of improvement

One other thing that helps companies fly clear of the sludge is having good business processes, and improving them all the time. The best Japanese companies, for example, are extremely good at logistics, both in their global operations and at home. Honda has a network of factories around the world, all hooked into the same supply chain. Each operates in the same way, so each is able to make any vehicle in the product range according to demand. This gives the company tremendous flexibility, thanks as much to slick logistics as to excellence in manufacturing.

Honda pays meticulous attention to detail to help ensure that its products are made on time. It has special data systems installed in each of its factories to monitor weather forecasts. These allow factory managers to talk in advance to parts suppliers about bad weather and how it might affect deliveries. They can decide what and when to stock up.

One of the best Japanese companies at logistics is Seven-Eleven, the largest convenience-store chain in the country. It is a rare example of a company whose business is largely domestic that is doing well despite Japan's deflationary environment. Its biggest strength is its custom-built information system that compiles extensive sales data (collected three times a day and analysed in 20 minutes). The system helps improve quality control and assists the company in pricing, product development and inventory management.

In the Japanese economy, any excess inventory can quickly translate into losses for firms that become too anxious to shift stock. For this reason, Kao has been working hard to improve its supply-chain management. Just as Toyota and other carmakers gained competitive advantage from honing their “just-in-time” delivery systems in the 1980s, so Kao has been steadily improving its inventory management—to the extent that it has saved around ¥10 billion ($85m) a year for the past 15 years. Companies such as Canon, Takeda Chemicals and Yamato Transport, the biggest parcel-delivery company in the country, are also strong in logistics and supply-chain management.

In many cases, these process improvements have gone against the grain. Japan is remarkably backward in its use of information technology. Its spending on IT jumped to 4.4% of GDP in 2001, from 3.9%. But the comparable figure for Europe was 5.2%, and for America, 5.3%. There is no shortage of computers on Japanese workers' desks, but many are still connected to old mainframes and run outdated software. Access to the internet is often available only via the one or two PCs around the office that are wired to the web.

Many of the firms that seem to have made the biggest productivity gains from IT are big exporters—car manufacturers and electronics firms. They are the ones with the global strategies that enable them to see what the rest of the world is up to.

The big new idea

One of the less obvious things that successful companies have done in hard times is to listen harder to their customers. They have become less intent on making things, and more intent on selling them. And that has meant being more thoughtful, not more forceful. Customers are likely to be going through hard

times too, and they may well show their appreciation of special consideration with more than a smile.

Sometimes this can force companies to shift away from their core business. Knorr-Bremse, for example, learnt from its customers soon after it had decided to focus on the brakes business that it was not going to be good enough just to make braking components. It had to develop complete systems that offered its customers more value. And that meant sharing more information with them.

Siemens too has had to adapt to the changing needs of its customers, as several of its markets have fundamentally changed over the past decade. Its transport division used to make just the electrical systems for trains. But now its customers want delivery of complete locomotives and carriages. So, to stay in the business, Siemens has had to broaden its operations, which it did by acquiring and integrating a dozen different companies. Loss-making a few years ago, the division is now profitable.

Similar efforts have been required to retain Siemens' leading position in other markets. During the second half of the 1990s it completely reshaped its ailing medical-equipment business, changing it from being focused on functions (such as marketing and R&D) to being focused on customers. Response times to customers, as well as the effectiveness of collaboration among staff, are now key determinants of performance. The effect has been dramatic. Profits last year were more than *euro*1 billion, and threats to move key production away from the company's historic base in Erlangen have been withdrawn.

Managers should take note. As all these examples—in Japan, Germany and elsewhere—show, a feeble economy is now a feeble excuse.

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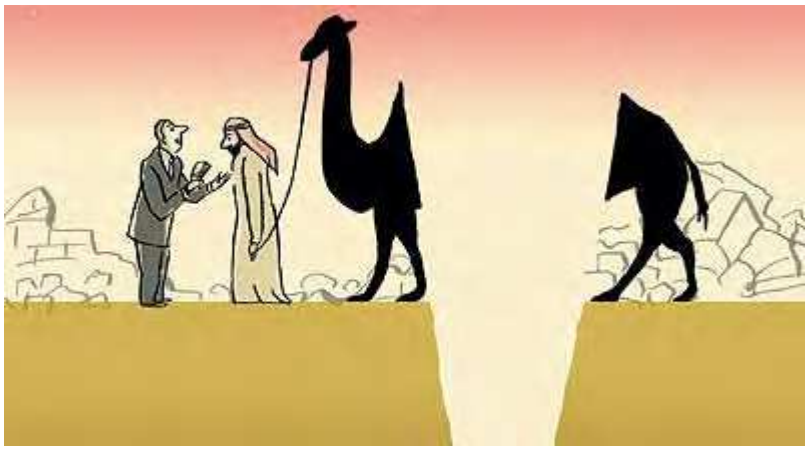
Iraqi debt

The cold calculation of war

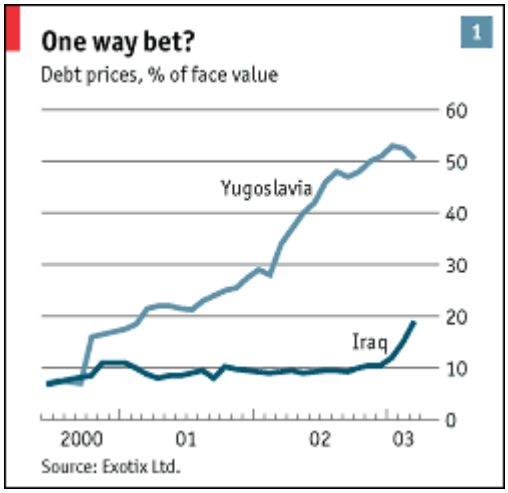
Apr 3rd 2003
From The Economist print edition



What war and its aftermath may mean for Iraq's creditors

DESPITE the murder of Zoran Djindjic, prime minister of Serbia, on March 12th, the secondary-market price of defaulted Yugoslavian government debt has remained buoyant, at 50 cents on the dollar. Speculative buyers of the debt, mostly loans already restructured in 1998, are gambling that the Serbian government will ultimately pay them more—pending, among other complications, the resolution of a dispute between the creditors' agent bank, J.P. Morgan Chase, and the National Bank of Yugoslavia. Their appetite has increased considerably since 1999, when the debt fetched only five cents on the dollar (see chart 1).

Will speculators one day show the same relish for Iraq's loans? Already, traders say, the secondary-market price of two big Iraqi loans has doubled, to around 19 cents on the dollar. Some believe that Iraq is a safer long-term bet than Serbia, because it has oil and is not (yet) hostage to a business mafia. This week a Serbian bankruptcy court sold a steel mill for $23m, ignoring the $1.7 billion the mill had borrowed from some now furious western governments and companies.



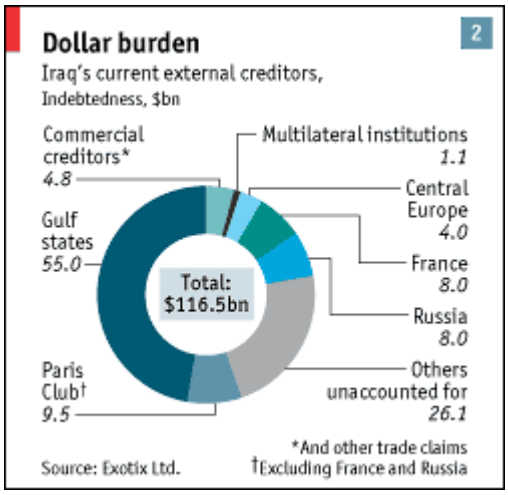
All depends on how long the war in Iraq lasts—and on how a future government deals with its legacy of debt. There is $116 billion of official and commercial debt, plus some $200 billion of reparation claims following Iraq's invasion of Kuwait in 1990 and the first Gulf war. Even for a country that might earn $25 billion a year from oil, it is an impossible burden.

The market view is that Iraq will negotiate the write-off of between 70% and 90% of the $116 billion. Traders also guess that the United Nations Compensation Commission (UNCC), which is handling unpaid reparation claims, will cut these to perhaps $40 billion. So Iraq's existing obligations could be reduced to between, say, $50 billion and $75 billion.

Who gets repaid, and how much, depends on which creditors a new Iraqi government would need most to help rebuild its economy. The creditors fall into three groups: the IMF and World Bank; governments that provided trade credits and bilateral loans; and private banks and companies (see chart 2). Iraq owes only $1.1 billion to the first group. Assuming they can be kept happy, the chances of other creditors depend on whether America sets up an officially funded reconstruction programme like the Marshall Plan

for western Europe after the second world war, or whether Iraq has to rely mainly on private funding. If the first, it will have to repay its official creditors, known as the Paris Club. If the second, it might follow Nigeria's example, repaying private creditors and ignoring official debt.

Above all, bankers argue, to return to the international capital markets, Iraq will have to show that it is at least willing to pay something towards its properly documented obligations. That would not include bills for sanctions-busting arms shipments, for example. But it would include bank loans, especially two big ones totalling $1 billion, syndicated in the 1980s, which have become a benchmark for Iraq's future creditworthiness. Although the price is only 19 cents on the dollar, a final repayment, including back interest, of up to 75 cents on the dollar is conceivable.



So far, there are few buyers—perhaps one or two a week—although the number of inquiries has soared lately, says Peter Bartlett of Exotix, an emerging-market-debt trading house. American entities are forbidden to trade. The buyers are mostly banks or a handful of funds that specialise in the debt of “pariah” states. Other Iraqi loans are traded too, such as letters of credit and other paper from the central bank, and two other banks, Rafidain Bank and Rashid Bank.

Trading, or even holding, Iraqi paper is loaded with traps. Its validity can expire every few years, according to the statute of limitations in various jurisdictions. Renewing it requires some acknowledgment from the borrower, and that was difficult even before the war. Assigning the debt from buyer to seller requires the borrower's assent, and the Iraqi banks have been unco-operative since 1988. The trick is to apply during public holidays, or when communications are down (as they are now), because the borrower's failure to respond within ten working days can be taken as agreement.

An alternative is to buy a sub-participation in a loan, but then the buyer takes on the credit risk of the intermediary as well. “All right if it's Deutsche Bank,” says one investor, “but not so good if it's a bank in Japan or the Middle East.” Prices are adjusted accordingly. There are long chains of sub-participations, compounding the risk of an already risky investment.

The complexity of Iraqi debt may not match that of Serbia, which is fraught with debt swaps between former Yugoslav republics and commercial debts that were turned into bilateral official lending. Still, it is complicated enough. The UNCC is working through reparation claims, but many of the biggest may take years to resolve. Omni Whittington, a Dutch firm that specialises in debt recovery from pariah states, is sceptical that prospects in Iraq will improve, even after the regime has been changed.

However, some commercial creditors have been able to unfreeze Iraqi assets abroad, except in America, and receive payment, as long as they demonstrate that the proceeds will not return to Iraq. Iraq's economy is centralised and reasonably simple. If the oilfields survive without heavy damage, there will be access to export earnings. The economy is almost bound to grow, albeit from a low base. That should encourage the purchase of speculative assets while they are still cheap. Vietnam may offer a better parallel than Serbia. In 1989, one pariah fund bought Vietnamese debt at four cents on the dollar. In 1995, it sold at 80 cents. That is not a bad return for a recovery that some thought inevitable.

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The Financial Services Authority

The gasman cometh

Apr 3rd 2003
From The Economist print edition

Sir Howard Davies is a hard act for Callum McCarthy to follow

Get article background

IN NOVEMBER 2001, when Enron was biting the dust, Callum McCarthy kept his nerve. There were calls for the government to intervene to prevent the collapse of Britain's newly created electricity-trading market, NETA, because it had lost its only big market-maker. But Mr McCarthy, the chairman of Ofgem, the gas and electricity regulator, insisted that the market would take care of itself. He was right.

This week the Treasury chose Mr McCarthy to succeed Sir Howard Davies in September as chairman of the Financial Services Authority (FSA), Britain's financial regulator. The FSA has been bad at ensuring that consumers know their dealings with financial intermediaries may be as exposed to chicanery as those with used-car salesmen. *Caveat emptor*, let the buyer beware, is a slogan that Mr McCarthy applied eagerly to the wholesale energy markets. He should do the same at the FSA.

Although his appointment confounded most forecasts, Mr McCarthy has good credentials. His background is uncannily close to Sir Howard's: same school, same Oxford college, and (same again) a year at Stanford Business School, followed by several civil service posts. Sir Howard worked for McKinsey and the bosses' union, the CBI; Mr McCarthy for Kleinwort Benson and Barclays. Sir Howard's leadership has depended on flamboyance and wit; Mr McCarthy is more of a technician, but as effective in public when necessary.

That has led him into some high-profile clashes at Ofgem. In creating NETA, he fought the vested interests of the power utilities and helped to bring down wholesale electricity prices by 40%. He insisted that British Energy, the languishing nuclear operator, should be allowed to fail, although he lost that particular battle. In a running skirmish with Brian Wilson, the energy minister, he has argued that renewable-energy schemes should be properly costed and subsidised rather than propped up by fudged electricity prices.

That readiness to do battle on the basis of markets, not ideology, should make Mr McCarthy a useful successor to Sir Howard. The FSA is increasingly encumbered by detailed rulebooks and legalistic procedures. Where Sir Howard mastered this complexity with apparent bureaucratic ease, Mr McCarthy may instead start to cut through the red tape. He will be assisted by a chief executive, not yet appointed. Sir Howard has done both jobs.

According to John McFall, chairman of the Treasury committee of MPs, which grills FSA officials (it once roasted Sir Howard), Mr McCarthy must perform a “balancing act” between politicians, the City and consumers. He will also have to play a leading role in shaping pan-European financial regulation. Paradoxically, the British financial super-regulator will be expected to resist plans for a single European super-regulator in its own image.

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About sponsorship

America's regional banks

Small is beautiful

Apr 3rd 2003 | NEW YORK
From The Economist print edition

Hard times have been good to America's smaller banks

THE mood inside America's big banks could hardly be worse, with relentless rounds of redundancies and niggling cost cuts. Step away from the better-known institutions, however, and the atmosphere changes dramatically. Regional banks' first-quarter profits are, on average, 17% higher than they were last year; delinquent loans remain modest; and deposits are pouring in.

This marks a big change from a dozen years ago, the last time America fought Iraq. Then a credit crunch deepened and extended a recession that left many borrowers, especially those who had bought commercial property, insolvent. This time, the good health of the regional banks is one reason why America's economy has, so far, remained more robust—notwithstanding a host of problems. Although demand for loans is modest, the banks at least have capital to back lending.

Since the early 1990s, consolidation has reduced the number of American banks by 40%. Most mergers occurred among firms with less than $100m of assets, typically small community banks. Many had been badly run.

The industry remains fragmented—there are still 8,000 banks, and the number is growing again—but it is in much better fettle. Return on equity has climbed from 8% at the end of 1990 to 15%, according to the Federal Deposit Insurance Corporation (FDIC), which guarantees Americans' bank deposits. This has happened even though the share of equity in the banks' capital has risen from 6% to 9%. What makes this transformation even more impressive, says David Ellison, a fund manager specialising in bank stocks at FBR Fund Advisors, is that, in the mid-1990s, equity was often inflated by goodwill after takeovers. During the past few years, this excess has been amortised away.

It is tempting to believe that the profits of regional banks have been driven up solely by America's mortgage-refinancing wave. Homeowners have switched to new loans as interest rates have plunged. Although the banks have been raking in loan-arrangement fees, Edward Najarian, an analyst at Merrill Lynch, thinks that these have been partially offset by the loss of servicing fees on the older loans. A bigger reason for their success, says Mr Najarian, is that they have avoided the worst effects of the recent slowdown, while enjoying the best of its by-products.

Unlike larger financial institutions, smaller banks had little exposure to the stockmarket or to the syndicated loans of large American companies. Consequently the bankruptcies of huge companies such as Enron and WorldCom largely bypassed the small banks. The small, private businesses that are their staple customers had no incentive to falsify their accounts or to issue stacks of dodgy share options. Regional banks have also steered clear of the other main area where credit is deteriorating, sub-prime lending (high-interest loans to borrowers with patchy credit).

Although small banks offer fewer products than larger rivals, they often do a better job. In New York, Commerce Bank has grown quickly by opening branches next to big, entrenched competitors such as Citibank, J.P. Morgan Chase, and HSBC. Commerce Bank then offers its customers longer banking hours and freedom from annoying fees. The result has been a surge in popularity.

Meanwhile, the decline in interest rates has been a great boon for commercial property, a core lending

business for community banks. At the same time, many Americans, fed up with Wall Street, have been pulling money out of the stockmarket and putting it into old-fashioned savings accounts at banks, even though they earn almost no interest. The banks have thus been raising money at little cost. Deposits at the medium-sized banks covered by Merrill Lynch have risen by 14% in the past year. These days, maybe, Americans are happy simply to put their money into an institution that not only accepts it, but also returns it.

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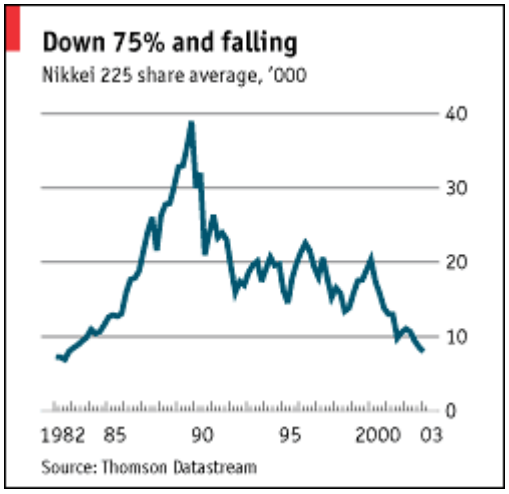
Japan's banks and life insurers

Still lousy

Apr 3rd 2003 | TOKYO
From The Economist print edition

A year-end health check on Japan's financial institutions

Get article background



JAPAN'S banks and life insurers have closed their books on another awful year. The banks have a huge weight of bad loans. The insurers are thought to be in still worse shape. Both are big equity investors, and their battering in the stockmarket continues. The benchmark Nikkei 225 stockmarket average fell by 27.7% in the year to March 31st, to 7,972.71, its lowest end to a financial year since 1982 (see chart).

Hironari Nozaki of HSBC Securities estimates that the top eight banks are sitting on ¥4.5 trillion ($38.1 billion) of equity losses, some recognised in the past year and some still unrealised. Guessing how much the big, mainly mutual life insurers have lost is trickier; but one analyst puts the unrealised losses of the top eight at between ¥1.5 trillion and ¥1.9 trillion.

This spells trouble for both industries. Realised or not, equity losses eat into banks' tier-one capital, of which the biggest eight have about ¥14 trillion. This implies an average capital-adequacy ratio of about 10%, still above the 8% that international rules require. However, the capital cushion is thinner than it looks. It includes ¥6 trillion of public funds that big banks received in 1998 (and are supposed to pay back) and ¥8.4 trillion of deferred taxes.

No wonder banks protested so fiercely last year when Heizo Takenaka, head of the Financial Services Agency (FSA), Japan's financial regulator, tried to cut the amount of deferred taxes that banks can count as capital. The banks have been raising capital frantically, ahead of the March year-end. The biggest, Mizuho, tapped its borrowers for more than ¥1 trillion.

The next checkpoint for the banks' books is end-September. Politicians in the ruling Liberal Democratic Party are putting forward new bail-out wheezes, such as returning up to 15 years' worth of back taxes to banks in the red. Others, including Mr Takenaka, want the Bank of Japan to buy equity-based exchange-traded funds, as a way of propping up the stockmarket.

The life insurers' basic problem is that they are locked into making high payouts when interest rates are ultra-low. The top seven think they lost ¥1.1 trillion in the year to March. Large falls in the stockmarket are an extra blow, because life insurers must recognise share-price losses of more than 50% in their profit-and-loss accounts.

As with the banks, politicians are mulling ways of helping the insurers out. One favourite idea is to force down guaranteed rates of return. That would mean breaking existing contracts, and it might not help much anyway. Nippon Life, the biggest company, bitterly opposes the idea of forcing the whole industry to cut payouts to protect the weakest. Yet if individual insurers were forced to reduce rates, many policies would surely be cancelled—and the weakest companies would not survive.

The fates of the banks and the life insurers are closely linked. Mitsuhiro Fukao, a professor at Keio University, estimates that a year ago the top life insurers held some ¥3.3 trillion-worth of bank shares. After Mizuho's recent share issue, they must have more now. Life insurers also held ¥4.5 trillion of banks' subordinated debt. In return, banks propped up life insurers with at least ¥2.5 trillion of loans. No

wonder Moody's, a rating agency, marked the end of the financial year by giving warning that this high level of interdependence increases systemic risks.

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About sponsorship

Star fund managers

Alpha males

Apr 3rd 2003
From The Economist print edition

Institutional fund managers find it hard to keep their high-flyers on board

THIS year has begun badly for Lazard Asset Management (LAM). On January 14th William von Mueffling, the “star” manager running the bulk of its hedge-fund business, resigned. LAM's bosses decided to replace him with Ben Guest, but Mr Guest left a few days later, to be followed out of the door by Robert Cope, Thomas Ellis, Rupert Tyer, Angus Parker, Simon Higgo and Jay Genzer. Last month Theodore Gillman, the head of LAM's private-client group, quit to run the fund-management business of First Albany Asset Management in New York.

Clients started to withdraw funds as soon as Mr von Mueffling's resignation became public. The defectors say that Lazard's $4 billion hedge-fund business has dwindled to less than $1 billion. Lazard will not comment on this figure. It wishes Mr von Mueffling well and says that its hedge-fund business is now being turned into “a team- and research-driven effort.” Still, the business seems to have been dented by the departure of a single star.

LAM is not the first institutional fund manager to find it hard to bed-in hedge funds. James Hedges of LJH Global Investments, a hedge-fund consultancy, says that it has never really worked in the past. In America, at any rate, almost all the firms that have tried—Putnam, Fidelity, Sanford C. Bernstein—have suffered the loss of stars sooner or later. Even bigger hedge-fund specialists often see their best men leave to run their own show. On April 1st, Perry Capital, a hedge fund with $5 billion under management, announced the departure of Christopher Hohn, manager of its European fund.

The ways of the hedge-fund business—trading aggressively, leveraging and short-selling (selling shares you do not own in the hope of buying them back at a lower price)—attract big egos. They often find it hard to defer to the hierarchy and etiquette of big institutions. More important, hedge-fund managers can earn more working on their own account than as part of a bigger firm. They usually charge an annual fee of 1-2% of assets, plus 20% of profits (but if they lose money in one year, they cannot charge clients' profits in a later year until the losses have been recouped). Left to their own devices, they keep all this; in a bigger firm, they must share some of the loot with more run-of-the-mill fund managers charging lower fees.

Fair shares

Compensation was the main reason for the clash between Lazard, the investment bank that owns LAM, and its hedge-fund team. Under Bruce Wasserstein, its boss since the start of last year, Lazard has begun to issue shares to its employees. The bank is said to have offered the hedge-fund crew about 2% of its equity. Mr von Mueffling thought his team deserved far more, having hauled in half of LAM's profits last year despite having only one-twelfth of its assets under management.

Lazard thought this greedy. After all, it said, Mr von Mueffling's team had relied on the firm's technical systems, back office, brand and marketing, not to mention a battalion of research analysts, who were keen to present their ideas to the hedge-fund maestro. And the hedge-fund people had based their demands on a bear-market year, when their business tends to shine compared with everyone else's.

In fact, most hedge funds have not done as well as they hoped during the bear market. With their focus on absolute returns, hedge funds promise to make money whether markets rise or fall, yet last year they returned only 3% on average, according to CSFB/Tremont, a provider of hedge-fund indices. An estimated 800 (mostly smaller) funds closed down. Even some bigger firms, such as Robeco, Bank Sarasin and Rourke Capital Management, wound down their hedge funds. Unsurprisingly, new investment

has slowed in the course of the year.

In that case, why should firms care whether hedge-fund managers stay or leave? In these difficult times, a fund manager who can still produce double-digit returns is even more sought after. A firm can profit from marketing a “star”, as Lazard did before the recent exodus. Mr von Mueffling's European Opportunities fund, launched in the autumn of 1998, returned 182% in its first year, thanks to a mix of beginner's luck and talent. Returns declined to double and even single digits, but last year bounced back to 17.4%, near the top of the hedge-fund league. Moreover, the rankings depend on the lead manager, not the team, however closely they work together. “If the top guy changes, we start a new track record,” says Joseph Nicholas, the head of Hedge Fund Research, a provider of indices for hedge funds.

Against the American trend, a few British firms have worked out a way of keeping hedge-fund managers and less exotic breeds under the same roof. “Gartmore and Henderson are an example of how to do it,” says Iain Jenkins at HedgeFund Intelligence. Gartmore, one of the pioneers of hedge funds in Europe, now runs an entire stable. Roger Guy, the star who runs the $1.3 billion AlphaGen Capella fund, has been with the firm for years.

Lazard, alas, did not keep its money-makers happy, and has become, unwillingly, a sort of hedge-fund incubator. The blow-up at LAM will probably spawn at least three new businesses. Mr Parker, Mr Higgo and Mark Pollard, another Lazard graduate, are setting up Jura Capital in London. Mr von Mueffling and Mr Cope will probably build a business once their gardening leave ends. Ditto Mr Guest. Now Mr von Mueffling and his pals are on their own, their successes—and failures—will certainly be of their own making.

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Economics focus

The perils of convergence

Apr 3rd 2003
From The Economist print edition

Countries joining the EU next year face a tricky path to the euro

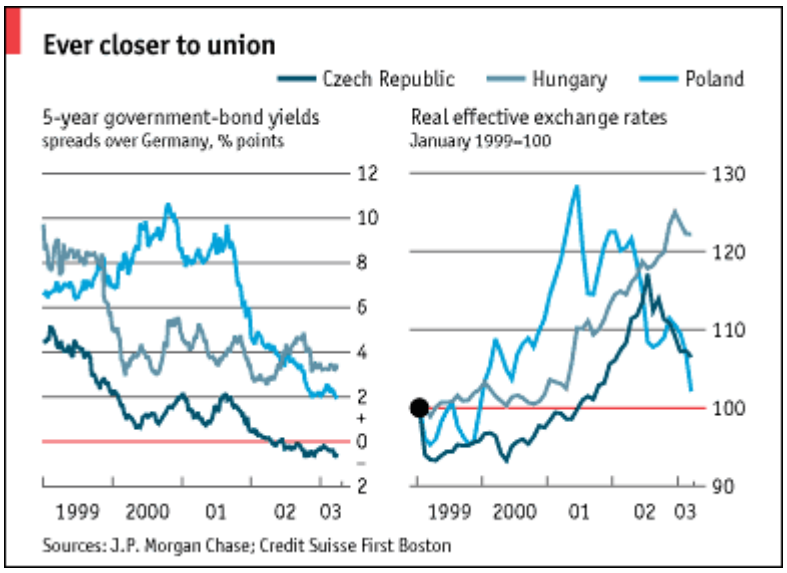
EVEN as they try to persuade their citizens to vote for membership of the European Union, the governments of the ten, mostly ex-communist, countries invited to join the EU in May 2004 are preparing for their next big challenge: adopting the euro. Many are eager to join, so as to reap the benefits of eliminating currency risk, lower interest rates than they now enjoy and (they fondly hope) faster economic growth.

In theory, the question is not if, but when, these countries will join the euro: unlike Britain and Denmark, which are in the EU but not the single currency, they have no Maastricht treaty “opt-out”. They are supposed to meet the same entry conditions as those set for the 12 current members of the euro area. As well as low inflation and long-term interest rates, budget deficits below 3% of GDP and government debt below 60% of GDP, that means they should spend at least two years in the EU's exchange-rate mechanism, ERM2, keeping their currencies within a 15% band either side of a central rate against the euro.

In practice, things may prove a lot fuzzier. The entry conditions, notably on debt and exchange rates, were fudged for some of the existing members. Several have since proved unable to keep their budget deficits below 3% of GDP. Few expect Britain, should it decide to join, to spend a preparatory two years in ERM2. Accession countries may thus be cut some slack. And should the EU's new members become reluctant to join, they cannot be forced to. Sweden, an EU member withno opt-out, has stayed out, though it will hold a referendum this September.

Financial markets expect the new members to join, although not before 2007. Spreads over German government-bond yields have tumbled (see chart). On some entry criteria, the hopefuls are in good shape: for instance, inflation is lower, in most of them, than it was in Italy, Spain or Greece a few years before they entered the euro. Against that, many have big budget deficits: over 5% of GDP in Poland, more in Hungary. Pressing too fast towards 3% might reduce the growth of national incomes that are still far below EU levels.

The European Commission and the European Central Bank (ECB) have urged the candidates not to rush into the euro, but to concentrate on structural reforms. They also think it essential that the EU's new members spend the prescribed minimum of two years in ERM2. Some policymakers in the region, and some academics, disagree. They see the regime as an outdated, booby-trapped framework that could trigger a currency crisis in central and eastern Europe. The turmoil in January in Hungary's exchange-rate system—in which the forint moves in the same band as it would in ERM2—bears this out. The central bank had to cut interest rates, at some cost to its inflation-fighting credentials, to stop the forint bursting through its upper limit.



Among ERM2's critics are the authors of a report*, originally written for the commission but published last month by the Centre for Economic Policy Research in London. The authors claim that the obligation to participate in ERM2 after the dismantling of all remaining capital controls on entering the EU will plunge the candidates into “an interim period [of] enhanced vulnerability before the safety of monetary union.” They rattle off a list of the currency crises of the 1990s, from upheavals in the forerunner of ERM2 to later crises in East Asia and Latin America. These forced several countries to jettison soft exchange-rate pegs, of which ERM2 is an example, in favour of either harder pegs (monetary union or currency boards) or fully floating exchange rates. If ERM2 came unstuck, it might not make countries ready for the euro, but rather delay their entry indefinitely.

Fighting Balassa-Samuelson

One problem is that accession countries can expect large capital inflows as investors bet on their convergence with the rest of Europe. This is likely to put upward pressure on exchange rates. But the inflows might then be reversed, sending the exchange rate down again. There is also the Balassa-Samuelson effect, which causes the real exchange rates of fast-growing countries to appreciate. Faster productivity growth in the tradable-goods sector leads to higher wages. Wages in the non-tradable sector then increase too, pushing up prices. The result is either a rising exchange rate—testing the limits of ERM2—or rising inflation, which would conflict with another condition of euro membership. The authors say that the Balassa-Samuelson effect has raised real exchange rates by perhaps 2% a year. These rates have strengthened, on average, in recent years, but have also fluctuated.

Granted, once inside ERM2 applicants may call on the firepower of the ECB to fend off speculative attacks and keep their exchange rates inside the set limits. But rather than test ERM2's robustness, the authors suggest that unilateral adoption of the euro (euroisation), without joining the euro area, might be a better bet. Many “closet unilateralists” in the region's central banks deride the ERM2 requirement, given the special treatment accorded to Italy and Finland, which were allowed to join the euro before spending two years in ERM2's predecessor. Both the commission and the ECB dislike the idea of euroisation, but the authors think their objections are overstated.

For some countries, such as Estonia, which has a currency board backed by the euro, such a quick transition may make sense. For others, ERM2 may be an invitation for markets to make mischief—especially if they believe that the central parity is not sustainable. Given the capital inflows (and maybe outflows) that these countries can expect, and given the likely upward pressure on their real exchange rates as they get richer, the best course for some might be neither unilateral euroisation nor ERM2, but to let the exchange rate float—ie, to wait and see.

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* “Sustainable Regimes of Capital Movements in Accession Countries”, by D. Begg, B. Eichengreen, L. Halpern, J. von Hagen and C. Wyplosz. Centre for Economic Policy Research, Policy Paper No.10.

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Correction

Apr 3rd 2003
From The Economist print edition

In our special report on insurance in the March 8th issue we said that Zurich Financial Services sold its North American operations last year. In fact, Zurich only sold its business in Canada. Sorry.

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Illegal drugs

Just say maybe

Apr 3rd 2003
From The Economist print edition

Reuters

For an example of how not to make good health policy, consider the international debate on drugs

Get article background

HOW should the world control the trade in and use of illicit drugs? As an issue of science and health policy, few questions matter more. In 1998 the United Nations General Assembly held a special session in New York which pledged the “elimination or significant reduction” of drug production and use within ten years. An evaluation of the targets set at that meeting takes place in Vienna this month, at a special ministerial session of the United Nations Commission on Narcotic Drugs. This gathering will hear that the world is no closer to meeting its goals than it was five years ago. But instead of asking such questions as whether the whole project may be misguided, the meeting will almost certainly decide to redouble international efforts to achieve the unachievable.

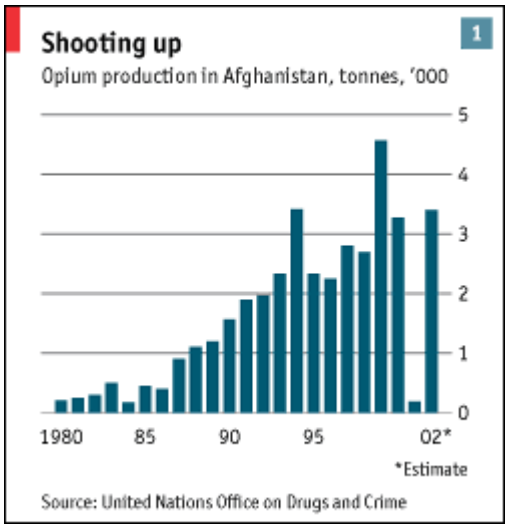
The framework for global drug policies is set by three UN conventions, dating from 1961, 1971 and 1988. Between them, these conventions set rules prohibiting, in almost any circumstances, the production, manufacture, trade, use or possession of potentially harmful plant-based and synthetic non-medical drugs, other than tobacco and alcohol. Crucially, these conventions go far beyond the bounds of most international treaties in the extent to which they dictate signatories' domestic policies as well as international relations. For example, the 1988 convention insists that signatories pass legislation to make the possession of drugs for personal consumption a criminal offence. That means they are, on the face of it, prevented from experimenting with the idea that controlled, permitted use may be less harmful than the side-effects of prohibition.

Plenty of non-governmental organisations (NGOs) and even some government ministers (in private, at least) now recognise that these treaties and the policies they encourage are the wrong way to tackle drug abuse. Unfortunately, those arguments look unlikely to make any headway in Vienna.

Turned off

The arguments for a different approach have grown stronger, not weaker, since 1998. The failure of the current policy has become much clearer. There is no sign that government intervention has cut supply, although it may sometimes divert it. For instance, the opium crop fell sharply in Afghanistan in 2001, under the Taliban government, but it rebounded last year after the American invasion (see chart). Meanwhile, according to Francisco Thoumi, a member of Colombia's Academy of Economic Sciences, Colombia's aggressive policies, aimed at wiping out the coca crop, have merely led to an increase in planting in Bolivia, where a coca grower almost won the recent presidential election, and in Peru. There is, says Dr Thoumi, no evidence of a decline in the availability of cocaine in the United States. Instead, the drug's purity seems to have increased.

There is plenty of evidence of broader failure too. The UN's meeting in 1998 set no benchmarks by which to judge progress. Success is judged by which programmes are in place, rather than by what they achieve. Thus a country that has plans to eradicate illicit crops can tick the appropriate box, even if the plan eradicates nothing. (And according to Anthony White, a British drug analyst, many countries have not even bothered to say which boxes they have ticked.) Back in the real world, the numbers tell a different story. Some recently released American figures show that more land in Latin America was planted with coca in 2002 than in 1998. Figures from the UN's Office on Drugs and Crime (ODC) show the retail price of heroin falling in the European Union (see chart overleaf). The use of Ecstasy among American and Canadian high-school students is rising. And so on.



In the light of this, a few governments—mainly European, but also those of Canada and Australia—are getting fed up with the treaties' emphasis on zero tolerance. Instead of prohibition, they are keen to emphasise “harm reduction”: to accept that drug-taking cannot be prevented, and instead to concentrate on reducing its consequences for health and crime.

The relentless rise of AIDS in intravenous drug users has been an important spur to this change of attitude. Switzerland has set up centres where heroin users can receive daily doses, together with medical treatment, and has seen drug-related deaths and crime diminish as a result. Britain may return to prescribing heroin to users, as it did until 35 years ago.

Britain has also skirted the intent of the treaties by deciding, as an experiment in part of London, not to enforce the law banning the possession of cannabis when an individual is carrying that drug for personal consumption. Jamaica, Spain and Portugal have gone further, extending such experiments to the whole country. And the Netherlands has long been noted for its tolerance of soft drugs.

So there is a case for considering change, and for allowing a coalition of the willing to experiment. Unfortunately, that is unlikely to cut much ice in Vienna. The main reason is the powerful anti-change lobby, led by the United States, whose attitudes and actions sometimes take on the ferocity of a medieval witch hunt.

Tuned out

The “no-change” lobby's watchdogs are the two bodies that actually manage the treaties: the ODC, which administers them, and the International Narcotics Control Board (INCB), which monitors breaches of them. In its annual report, published in February, the INCB attacked the “crusade” to encourage harm reduction. It singled out Britain's approach to cannabis for special condemnation. The INCB did this despite having recently received legal advice from the ODC that harm-reduction approaches might conform with the UN treaties. The INCB attack drew a furious retort from Bob Ainsworth, a British minister, who complained about “the alarmist language used, the absence of any reference to the scientific evidence on which that decision was based, and the misleading way in which the decision was presented by the INCB”.

As for the ODC, its culture is inherited from the UN International Drug Control Programme (UNDCP), which it recently swallowed. That body was a byword for bad management and internal strife. Two years ago, one of its senior staff described it as a “snake pit” (and then left). Pino Arlacchi, its last executive director, was eased out after an auditors' report exposed serious mismanagement, and a lot of other top

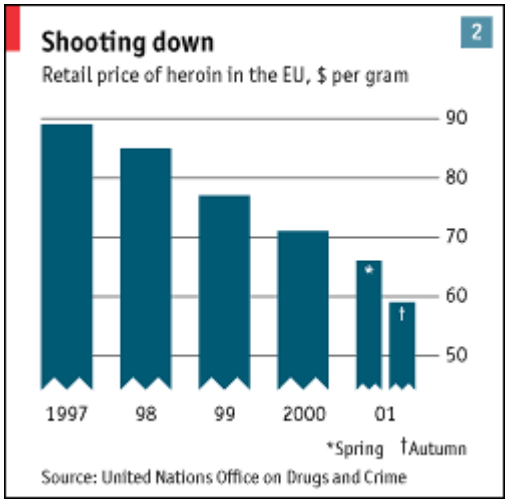
staff have either departed in despair or been pushed out. In one of several articles on the forthcoming meeting in the latest issue of the *International Journal of Drug Policy*, Cindy Fazey of Liverpool University, in England, describes the power wielded over the organisation by the main donors, especially the United States. In her time, she says, “punishment postings were not infrequent, to places such as Yangon, Myanmar; Lagos, Nigeria; Dakar, Senegal...the result is that many UNDCP staff are in constant fear of their jobs.”

The ODC now has a new director, Antonio Costa, a former secretary-general of the European Bank for Reconstruction and Development. So things may change. But whatever the international agencies think, plenty of countries that have signed the three conventions are vehemently opposed to any liberalisation.

America is easily the most powerful of these. Under the presidency of George Bush, says Ethan Nadelmann, executive director of the Drug Policy Alliance, an American lobbying group, prospects for even modest reform are bleaker than they were under his father's presidency. America has the power to make life miserable for any developing country that does not share its enthusiasm for suppressing drugs, and does not hesitate to use it.

America is not alone, though. Islamic countries share its hostility even to the legalisation of cannabis, as do Russia, China and Japan. Even within the European Union, member states are split in ways that have made it impossible for the organisation to form a common ministerial view. Spain, Portugal and the Netherlands may be liberal, but Sweden has long backed zero tolerance. The governments of Italy, Ireland and France are also tough-minded. Jacques Chirac, in particular, is an old anti-drug warrior.

In early March Greece, which currently holds the EU presidency, called a conference to discuss EU views in advance of the Vienna meeting. It was composed of a mixture of national representatives, free-floating experts and NGOs. The conference, at which rationality mainly prevailed over ideology and rhetoric, ended in anger. The French delegation savaged the Greek hosts for daring to allow government delegations to mix with liberal opinions, and for producing a conference report that recorded both doubt and debate. That bodes ill for Vienna.



Dropped in?

It is just possible, though, that the impasse can be broken. One striking change since 1998, notes Mike Trace, Britain's former deputy drug tsar, is that NGOs have begun to moderate their demands. Five years ago, these lobbyists clamoured for an end to all restrictions on drug use and trade, encouraging defensiveness on the other side. Now, the debate has become more sophisticated, with the lobbyists willing to explore other, more flexible, approaches.

One possibility, suggests Martin Jelsma, of the Transnational Institute, a Dutch think-tank, is the creation of an informal alliance of countries keen on more flexibility. Three groups might come together: Commonwealth countries such as Britain and Canada that want a pragmatic approach to cannabis; European countries such as Germany and Switzerland that are keen on harm reduction and open debate; and Latin American countries such as Brazil and Bolivia which are desperate for a better way to deal with the curse of cocaine. But sooner or later, such an alliance would still have to deal with the conventions. These have been signed by well over 100 countries, and cannot lightly be altered or set aside. The path to a rational drug policy is likely to be a long one.

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About sponsorship

Quantum computers

Dream code

Apr 3rd 2003
From The Economist print edition

Programming languages for quantum computers are now being written

Get article background

THERE are times when putting the cart before the horse is actually sensible. Quantum computers, which rely on the arcana of quantum mechanics to do many computations in parallel, are a long way from actually being useful. But researchers are already trying to work out how to write programs for these almost non-existent devices, in the belief that learning how to do so might help engineers to design the computers in useful ways. A paper by Stefano Bettelli of Paul Sabatier University in Toulouse, France, and his colleagues, which has just been accepted by the *European Physical Journal*, describes the latest effort to come up with a quantum programming language.

The basis for existing “classical” computers is the binary digit, or “bit”, which can have a value of either 0 or 1. In a quantum computer, bits are replaced by “qubits” which are in a “superposition” of states—partially 0 and partially 1. It is this superposition that allows calculations to be performed in parallel. Measuring the value of a qubit causes it to collapse into one of the two classical bits, 0 or 1. In a well-organised quantum computation, that should not happen until it becomes necessary to find out what one of the values actually is.

That, at least, is the principle. Converting it into practice will be tricky. Dr Bettelli and his colleagues have, nevertheless, tried. The key elements of their language are things called quantum registers and quantum operators. The quantum registers are ways for a program to interact with specific qubits. They act as “pointers” to the locations of qubits within a machine. Those qubits can then be manipulated by the program.

The manipulation itself is done by the quantum operators. These are the equivalent of the logical operators, such as “and”, “not” and “or”, that are the basis of classical programming (in which an instruction might say “when A or B and not C are true, do D”). Quantum operators rely on what are known as unitary transformations (the origin of the name is buried in the algebra of matrices). The trick is to find a way to describe, in a manner useful to computer scientists, the unitary transformations that underlie a program. Dr Bettelli has managed to do it using object-oriented programming—long a buzzword among software developers.

Object-oriented programming works by combining both commands and data into individual bundles known as objects. These objects can be used to bridge the gap between the classical and quantum worlds. Because a working quantum computer is likely to be a specialised portion of a larger classical computer, any successful language will have to be able to handle registers and operators in ways that allow them to be integrated with old-fashioned classical computations. Representing a unitary transformation as an object makes it fairly simple to translate programming directives at the classical level into physical control instructions at the quantum level. Dr Bettelli's language should do this.

It is still early days, clearly. But it is worth recalling that much of the past half-century's progress in classical computing was both predicted and made possible by such prescient theorists as Alan Turing and John von Neumann. Although programming languages may change a great deal before usable quantum computers can be built, it is worth constructing the theoretical underpinnings now. Quantum programmers would do well to heed the words of Dwight Eisenhower: “I have always found that plans are useless, but planning is indispensable.”

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Forensic science

Don't rain on my parade

Apr 3rd 2003
From The Economist print edition

Another strong reason to distrust identity parades

THE value of identity parades is questionable. For a start, the number of people in a normal line-up means that the chance of picking the suspect by chance is a lot higher than a statistician would consider safe for any scientific test. Then there is the question of whom it is meaningful to put in a parade besides the suspect. But most dangerous of all is the risk that a witness may be "led" into a choice by remarks, whether chance or deliberate, by somebody involved in conducting a parade.

This last risk, at least, is well recognised. But there is a widespread assumption that, an identification having been made from a parade, subsequent banter can do little harm. Not so. According to Gary Wells and his colleagues at Iowa State University, even remarks made two days after an identity parade might compromise a witness's eventual reliability in court.

Dr Wells's research, just published in the *Journal of Experimental Psychology*, took more than 250 subjects and showed them a video of what appeared to be a terrorist planting a bomb. At one point, the camera focused in so that the man's face was clearly visible. The subjects were then shown a photographic line-up of six people who looked similar to the "bomber". In fact, none of these photos actually was of the bomber. Nevertheless, with a bit of encouragement to make some sort of choice, every one of the subjects identified one of the pictures as being of the bomber—itself an observation that raises questions.

Having made a choice, the subjects were assigned at random to one of a number of groups, each of which was treated differently. Dr Wells wanted to find out both the effects of feedback, and how they changed depending on when the feedback was given. The three sorts of feedback were: none at all; a confirmation that the subject had picked the correct individual; or an observation that the wrong individual had been picked. This feedback might be given either immediately, or at a second session which took place 48 hours later. The subjects were also asked (again, either immediately, or after 48 hours) a series of questions about how confident they were in their choice, how good a view they had had of the incident, how much attention they had paid, and so on.

Dr Wells expected, from previous results, that those who had immediate confirmation that they had picked the suspect would be more confident about their decision than those who had not. He was not disappointed in this expectation. The new and worrying result was that exactly the same thing happened even when the first "confirmation" that a subject had chosen correctly happened 48 hours after the identity parade. That, if it is confirmed by subsequent research, has great implications for the reliability of witnesses in trials, since it is easy to design codes of conduct that prevent immediate feedback, but harder to devise ways of stopping details slipping out later.

This matters because research has shown that, in America at least, it is not only the fact that a witness picked out a suspect in an identity parade that matters in court. The confidence with which the witness defends the choice under cross-examination sways verdicts. Identity parades have long looked unsatisfactory as material evidence. This result is another reason to question them.

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About sponsorship

Soviet Russia

Worked to death

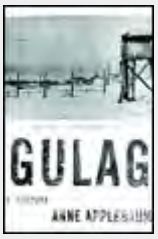
Apr 3rd 2003
From The Economist print edition

Rex Features

Is there a moral equivalence between Hitler's concentration camps and the Russian Gulag? A new book looks at the singular history of Stalin's labour camps

IN POST-COMMUNIST Prague you can buy Soviet mementoes: red stars, hammers and sickles, portraits of Lenin. So at least Anne Applebaum discovered one day while crossing the Charles Bridge. She reflected that selling swastikas and portraits of Hitler would rightly be considered an outrage. What was the difference? Why does western public opinion seem so indifferent towards the legacy of the Soviet concentration camps while continuing to regard the Nazi ones with justified abhorrence? This question was one of the impulses that led her to write the history of the Gulag.

Gulag: A History
By Anne Applebaum



Doubleday; 736 pages; $35. To be published in Britain by Penguin/Allen Lane in May 2003

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The two penal systems were similar in their end result: millions of deaths. But there were many differences in their origin, purpose and way of operating. The first Soviet camp, the former Solovki monastery on islands in the White Sea, was initially conceived as a remote place where the Reds' enemies could be isolated. Only gradually were its inmates compelled to engage in productive labour, felling trees and building roads. Then, as the Soviet Union launched a crash programme of industrialisation in the late 1920s, the planners decided that forced labourers could usefully be made to open up remote and forbidding areas of the country, where free workers would not settle. In short, they could become part of the planned economy. So coalfields were developed at Vorkuta, in the Komi Republic in the arctic north of European Russia. In the Far East, the Dalstroi camp complex exploited the gold and platinum deposits of the Kolyma region.

The archives demonstrate that Stalin and the Politburo paid regular close attention to both, in particular to Dalstroi, whose gold was vitally needed to finance the import of western technology during the industrialisation drive. The records show them discussing it in the accountant's bland language of input, output and profit, paying no attention to human cost.

By the 1930s the human cost could be ignored because the labour camp inmates, or *zeki*, were branded as enemies of the people—it was an offence to call them comrades—and were therefore expendable. Mass murder was not actually an aim of the system, as it was in Nazi Germany, but the imperatives of forced industrialisation, combined with the stigmatisation of those arrested, made it possible to impose

inhuman work conditions which invariably killed many.

The only way to motivate convicts with no prospect of early release was to feed well those who worked hard. Those who failed to fulfil their targets had their rations cut; weakened by inadequate nutrition, they fell even further behind, and the resultant vicious circle was a death sentence in all but name. In time, the Soviet leaders realised that, even in a populous country, such heedless consumption of human resources was damaging. From 1939, when Stalin's chief of the secret police, Lavrenti Beria, was put in charge of the Gulag empire, the *zeki* were given adequate food and medical care when possible, not out of humanity, but because healthy workers were more productive than sick ones.

Ms Applebaum, who covered eastern Europe for *The Economist* during the collapse of Soviet-run communism, devotes an effective chapter to the camp guards. Most of them behaved with appalling callousness to their charges, especially in the cattle trucks used for rail transports and in the convict ships of the Far East. What explains their behaviour? They were not all sadists, but they were poorly educated and some had been criminals. They belonged, for the most part, to the lowest rung of the NKVD, a forerunner of the KGB, and lived in conditions only slightly better than those of the *zeki* themselves.

Years of state propaganda had taught them that the *zeki* were not fully human: the term “sub-human” was not used, as it was by the Nazis, but “enemy of the people” was intended to be almost as demeaning, and was combined in propaganda with terms like “vermin”, “filth” and “poisonous weeds”. To treat prisoners well meant performing duties conscientiously, taking trouble, sometimes intervening to restrain criminal thugs—and most of the guards saw no point in thus exerting themselves for charges whom they regarded as worthless. It is as well to ponder this dehumanisation of ordinary people, for this is how atrocities come about.

Ms Applebaum has some distinguished predecessors in writing the history of the Gulag system, notably Robert Conquest and Alexander Solzhenitsyn. She can well stand comparison with them, and in some respects supersedes them. She takes the story right up to the end of the Soviet period, and she has made good use of published material and archives which have become available only in the last ten years or so. They include those of Memorial, the association set up in the late 1990s to retrieve and make known the full truth about the Soviet penal system and its victims. Some of her most interesting sources, though, come from the state archives, notably the long and detailed reports of the NKVD's Gulag Inspectorate of the 1930s and 1940s. These were as frank as Mr Solzhenitsyn was to be decades later in the “The Gulag Archipelago” in revealing the deficiencies and abuses rife within the system, and they recommended ways to curtail them, in the interests of higher productivity. Usually nothing effective was done at the time, but those reports left a rich resource for the historian.

“Gulag” is lucid and well-researched, and its moral message is clear without being obtrusive. It should become the standard history of one of the greatest evils of the 20th century.

Gulag: A History.
By Anne Applebaum.
Doubleday; 736 pages; $35. To be published in Britain by Penguin/Allen Lane in May 2003

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Diet

Grandma was right

Apr 3rd 2003
From The Economist print edition

SUPPOSE you are a fat New Yorker. Suppose, furthermore, that you are increasingly susceptible to heart disease and you have to get the pounds off. Time is not on your side, and there are more than 25,000 diet books in print. Where do you go to find dependable counsel? The man you need, many cardiac specialists will tell you, is a New Jersey doctor named Joel Fuhrman who specialises in nutrition.

Dr Fuhrman dislikes what he regards as faddish regimes: Barry Sears's “zone diet”, Dr Atkins's low-carb solution and James D'Adamo's controversial advice for people with different blood groups. Nor is he a fan of the USDA diet recommendations that, he says, have created the paradox of a population that is overfed but undernourished.

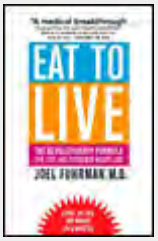
The pitfall of most diets, Dr Fuhrman argues, is that they tend to regulate macronutrients—proteins, fats and carbohydrates. The focus of “Eat to Live” is on micronutrients—vitamins, minerals, antioxidants and phytochemicals that promote health. The goal of a healthy diet, he says, is to get the most micronutrients from the fewest calories.

Dr Fuhrman suggests almost eliminating fats and starches in favour of greens, beans and fruit. His regime even works if you don't do a lot of exercise. This reviewer, who has become something of an expert on diets over the years, lost ten pounds (4.5 kilos) in one month; the norm, Dr Fuhrman claims, is 15. Empty calories from soft drinks, dairy products, meat and starches or processed foods with little to no micronutrition are easily converted to fat and extra poundage. So-called “2 percent” milk claims to be a diet food, but 35% of its calories come from fat. On the other hand, green vegetables are an excellent source of protein as well as antioxidants that reduce risk of cancer and heart disease. By weight, the amount of protein they contain is insignificant, but in terms of calories broccoli is 45% protein, while a cheeseburger contains only 21%.

Sit up, George Bush senior, scourge of broccoli. Without the protein in greens, how else could your Texan cattle develop all that tasty muscle?

Eat to Live: The Revolutionary Formula for Fast and Sustained Weight Loss.
By Joel Fuhrman.
Little Brown; 224 pages; $23.95. Piatkus Books; £6.99

Eat to Live: The Revolutionary Formula for Fast and Sustained Weight Loss
By Joel Fuhrman



Little Brown; 224 pages; $23.95. Piatkus Books; £6.99

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Tibet

Flights of fancy

Apr 3rd 2003
From The Economist print edition

“I HAVE never”, wrote Basil Gould, a frontier official of the British empire, of the 14th Dalai Lama, “seen anybody assume more complete and natural control of great assemblies.” Back in London, in the margins of Gould's dispatch, a colleague dismissed this with a scribble: “flight of imaginative fancy”. The year was 1940 and the boy, after all, was only five years old. Yet Gould was right. The Dalai Lama, now approaching 70, draws crowds second only to the pope. Born in western China, though exiled from there since 1959, he is more famous than any Chinese. He has few critics other than China's communist government and, in the West, Christopher Hitchens, a pugnacious commentator. He is, as one American magazine puts it, “the coolest spiritual-leader daddio around”.

Thanks in big part to the Dalai Lama's own magnetism, the issue of Tibet, as Patrick French recounts, went in a decade from “being obscure to cult-fashionable to mainstream”. Tibet's suffering has been internationalised, but it has also been commoditised. Buddhist monks preside at Hollywood fund-raisers. Westerners arrive in Dharamsala, home in India to the Dalai Lama and the optimistically named “Government of Tibet in Exile”, to live out their own imaginative flights, in varying states of fancy dress. This is the export version, the “mind's Tibet”, and for many people it is preferable to the real thing. Foreign advisers, one Tibetan writes, batten themselves on to the Dalai Lama's court with the “tact and sensitivity of lampreys”.

Tibet, Tibet: Dreams and Memories of a Lost Land
By Patrick French

HarperCollins; 324 pages; £20. To be published in America by Knopf in October

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If this appears to have done the Dalai Lama little material good—for instance, Dharamsala got nothing but the promise of a few computers for his appearance in Apple's “Think Different” advertising campaign—the spiritual leader is unconcerned. “I am”, he says, “what you want me to be. I am a screen-saver for computers. I don't mind.” But Mr French's contribution is to show how the West's dreams and projections have resulted in little of benefit for Tibet itself. One Tibetan tells Mr French that campaigning for an independent Tibet may make western protesters feel good; but “for us, it makes life worse. It makes the Chinese create more controls over us.” As a Tibetan nun puts it: “If you stand up, you bump your head, if you sit down you bang your arse.”

AP

Screensaver to the stars

Mr French, a magnificent biographer of Francis Younghusband and chronicler of India's road to independence, goes over a lot of the same ground recently covered by more thorough historians of Tibetan lands and of China's relations with them, notably Melvyn Goldstein and Tsering Shakya. His real contribution in this book, on the other hand, is the frank questioning of his own mind's Tibet and the growing scepticism with which he looks at the Tibet lobby's own claims.

It does not help the cause that much of the propaganda it trades with the Chinese communists is false. The number of Tibetan deaths usually attributed to the Chinese since 1950, at 1.2m, is grossly inflated. During the evil of the Cultural Revolution after 1966—Tibet's greatest tragedy—it was chiefly Tibetans themselves who smashed their own temples and shrines, something the lobby glosses over. Its insistence that Tibet proper includes vast swathes of western China that were never under Lhasa's direct rule is surely unhelpful, as is the refusal to acknowledge that Tibet's rulers centuries ago abdicated responsibility in favour of foreign influence. Some of China's historical claims, as it happens, are not entirely groundless while those of the Tibetan

lobby have sometimes been less than honest. During the course of his research Mr French resigned as a director of the Free Tibet Campaign.

Above all, Mr French understands that any settlement of the Tibet question—and you might as well forget full independence—will not happen without a more confident, accountable government in Beijing. Until then, Tibetans working within the Chinese system have a better chance of safeguarding what is left of Tibetan identity than can any amount of righteous outrage in the West.

Tibet, Tibet: Dreams and Memories of a Lost Land.
By Patrick French.
HarperCollins; 324 pages; £20. To be published in America by Knopf in October

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New fiction

Toothmarks

Apr 3rd 2003
From The Economist print edition

FOR a few years in the 1920s the biggest star of the hugely popular Ringling Brothers Barnum & Bailey Circus was a tiger trainer from the backwoods of west Kentucky called Mabel Stark. With a flick of her wrist or a tilt of her comely head she could persuade 16 snarling and terrifyingly unpredictable Bengal tigers to jump through hoops or pile on top of one another to form a great orange and black pyramid.

But Mabel's most popular routine was much more intimate than that and never failed to leave the audience slack-jawed with amazement. It involved just the fearless trainer and her favourite tiger, a magnificent 500-pound brute named Rajah.

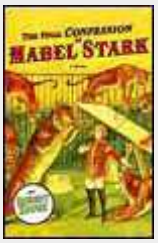
As Mabel explained in her own words: “When I turned and called him he would come up on his hind feet and put both feet around my neck. Pull me to the ground, grab me by the head, you know a male tiger grabs the female by the neck and holds her and growls till the critical moment is over. So in this fashion Rajah grabbed me and held me. We kept rolling over till he was through, and while the audience could not see what Rajah was doing, his growling made a hit.” Mabel's costume for this act was a suit of protective leather. It was white so that the audience couldn't see Rajah's semen splashed all over her back as she bowed to accept their applause.

Drawing on letters and old newspaper clippings, Robert Hough has used his imagination to fill in the gaps and work up Mabel's extraordinary life story into a tremendously enjoyable novel. He follows her from her early days as an exotic dancer through those heady years as the world's most famous tiger trainer and a string of marriages and love affairs to an undignified semi-retirement in California, where she found herself washed up and bitter in the late 1960s, her body criss-crossed with scars from 50 years of maulings.

“The Final Confession of Mabel Stark” is not a feat of virtuoso ventriloquism like Peter Carey's “True History of the Kelly Gang”. But Mr Hough has found a voice and tone—prickly and pathetic, sly and wounded—that fits Mabel as snugly as her soiled leather suit.

The Final Confession of Mabel Stark.
By Robert Hough.
Grove Atlantic; 440 pages; $24. Atlantic Books; £10.99

The Final Confession of Mabel Stark
By Robert Hough



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British naval history

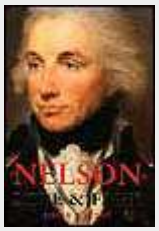
Winner takes all

Apr 3rd 2003
From The Economist print edition

“IF IT be a sin to covet glory,” wrote Horatio Nelson to Emma Hamilton in February 1800, misquoting Shakespeare's “Henry V” slightly, “I am the most offending soul alive.” The middle child of a large family, who lost his mother when he was nine, Nelson so craved recognition and fame that he was prepared to sacrifice his limbs, his health and ultimately his life to win it.

As we approach the bicentenary of his death at the Battle of Trafalgar on October 21st 1805, there are many signs that his fame is as strong as ever. Nelson would have been delighted that he was voted on BBC television as one of the ten “Great Britons” and flattered to share the honour with two former members of the royal family. An assiduous promoter of his own public image, he would have relished the excitement when staff at Britain's National Maritime Museum recently unearthed a sketch, roughly drawn in his own hand that demonstrated the tactics he intended to use in his next battle. Never one to undervalue himself, he would certainly have appreciated the fleet of new biographies that are due as we approach 2005.

Nelson: Love & Fame
By Edgar Vincent



Yale University Press; 656 pages; $35 and £25

Buy it at
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Edgar Vincent's is the latest of these vessels to take to the water. Nelson's fame and his lifelong quest for it is one of his main themes. With over 600 pages of good-quality paper, his is a massive three-decked battleship of a book, in general handsomely produced, but let down by some poorly designed colour plates, including a number of reversed images. Mr Vincent's text is an eloquent retelling of the familiar story: especially strong on psychological insights and illuminated by passages of vivid writing. The evocation of the horror of the sudden destruction of the French flagship *L'Orient* at the Battle of the Nile is particularly well done. Less happy are his frequent forays into invented speech, as when Nelson, approving Lieutenant Pasco's amendment to his famous Trafalgar signal, suddenly starts speaking like Captain Picard of the *Starship Enterprise*: “Make it so”.

Mr Vincent's other major theme is Nelson's attractiveness. He wants his readers to understand how Nelson achieved his remarkable feats of leadership and why so many of those who came into contact with him loved him. While giving just weight to Nelson's faults, he nonetheless creates a persuasive image of a charismatic man who genuinely cared for people. As such, his book is a useful counter-balance to Terry Coleman's “The Nelson Touch” (Oxford University Press, 2002), which portrayed Nelson essentially as a ruthless killing machine.

The publishers claim that the book is based on extensive research in primary sources. However, the footnotes reveal that Mr Vincent has in fact drawn his material predominantly from the heavily edited Victorian editions of Nelson's correspondence, rather than from original manuscript sources. It would appear, too, that he was not aware of the large body of fascinating new material that is currently being unearthed by Nelson scholars in archives in Britain and in America, and which is bringing some intriguing light and shade into aspects of the traditional story.

As a result, this is not a book with startling new revelations. It relies for much of its effect on its author's personal insights, based on a lifetime's study of his hero. We must look to future biographers for the deeper analysis and revised narratives that the emerging new material demands. But in the meantime, we can enjoy Mr Vincent's passionate, and unashamedly partisan, celebration of Nelson's life and career.

Nelson: Love & Fame.
By Edgar Vincent.
Yale University Press; 656 pages; $35 and £25

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About sponsorship

Cai Guo-Qiang's installation art

Playing with fire

Apr 3rd 2003 | GHENT, BELGIUM
From The Economist print edition

Firework chaos theory from a latterday Prospero

IT IS unusual for an exhibition to open with the audience being evacuated and firemen rushing in—even in the weird world of contemporary art. Men in hard hats are the only eyewitnesses when Cai Guo-Qiang lights his massive gunpowder portrait of the founding director of Ghent's contemporary art museum where this event takes place. Crowds, including the director himself, watch on an outdoor video monitor as his face goes up in flames. Afterwards Mr Cai and his assistants damp out the fire using long poles tipped with sponges, and then smudge the lines of ash so that the portrait looks like a huge charcoal drawing on the wall of the museum's reception hall.

Back inside, there is an indoor river, a nude woman bathing in a suspended glass “sky bath” and a mini-rollercoaster, all part of a Cai retrospective in Ghent, a half-hour train journey from Brussels. Too much fun to be art? Perhaps, but Mr Cai wants viewers to do more than look—they must participate. In yak-skin boats, they float down the river that he has fashioned from bamboo and fibreglass. Above them hang sculptures from the past decade of his career. Upstairs, Mr Cai has built a mini rollercoaster in a cavernous gallery, on whose ceiling is painted Mr Cai's history of Belgian art—images from the city's famous Ghent altarpiece and iconic works by Magritte and Broodthaers. Riding along, viewers are suspended between the ground and an art-filled sky. The rollercoaster places them at the centre—between heaven and earth, chaos and control.

Mr Cai's intention is to connect people with the cosmos. Nothing expresses this better than his trademark explosion events. The momentary chaos and creative destruction of explosions have long fascinated him. Ten years ago, he extended the Great Wall of China by ten km with a wall of fiery explosions visible from space, entitled “Project for Extraterrestrials No. 10.” The performance pictured below is at Kyoto city hall, and it appears in a new book, “Cai Guo-Qiang” (Phaidon). Like a modern-day Prospero, Mr Cai uses gunpowder to harness the elements. His explosions tap into a primordial human attachment to fire and to what he sees as our genetic memories of the Big Bang.

Based in Manhattan since 1995, Mr Cai was born in 1957 in Quanzhou, a coastal town in eastern China, where he grew up to the sound of gunfire across the Straits of Taiwan. Gunpowder, historically, was used as a means of communication. Fireworks in China announce births, marriages and deaths, and were once thought to deter evil spirits. The Chinese word translates as “fire medicine”; an alchemist invented it accidentally while concocting a health cure. “Now we turn on our television sets every morning and see its more destructive use. I keep thinking how similar the bombs in Iraq look to my art. It's not the fault of the medium, it's the intention.”

The son of a calligrapher, Mr Cai wanted to be an artist but chose to study drama because Chinese art

schools taught only propaganda painting. Once there, he was drawn to the theatricality of productions. “Chinese theatre taught me to consider how the audience perceives my work. Theatre always takes different forms depending on the script. That's the way I see my art. It's not about a particular style. It's about an attitude.”

The most moving work in Ghent is a video montage of mushroom clouds above a sandpit filled with crabs. Protected by water, crabs were the only creatures to survive Hiroshima. Mr Cai sees the mushroom as the modern equivalent of the Great Wall. “Both were deterrents; both were stunning, visible symbols of power”. Mr Cai conceived this show long before the Iraq war, but he is worried by the idea of smart bombs. Explosions create chaos. They are by nature uncontrollable; that is what attracts him to them as an artist. “No matter how carefully you prepare an explosion,” he says, “when the elements of heat, wind, speed and height combine, explosions are still unpredictable. Nothing ever turns out the way you expect, which is ideal in art but perhaps not in war.”

Cai Guo-Qiang, “An Arbitrary History”, Stedelijk Museum voor Actuele Kunst (SMAK), Ghent, until June 1st. Catalogue published by Seuil, *euro*25

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Rem Krasilnikov

Apr 3rd 2003
From The Economist print edition

Rem Krasilnikov, Soviet spycatcher, died on March 16th, aged 76

IT WAS a good name, was Rem, for a loyal servant of the Soviet Union to have, an acronym of *mirovaya revolyutsiya*, or “world revolution”. In 1927, when Rem Krasilnikov was born, the memory of the Russian revolution was still fresh enough in the minds of parents for them to want to commemorate it in the names of their children, rather as numerous Winstons were born in Britain after the second world war. Rem's father was an officer in the NKVD, a Soviet security organisation that was a forerunner of the KGB, so calling his son Rem would be more than a sentimental gesture; it would have the approval of his superiors. And it can be assumed that Krasilnikov senior, aware that security was tightening throughout the land, believed that his son's distinctive name would help to protect him in the difficult times ahead. (Later, three NKVD chiefs were shot in succession on Stalin's orders, as well as many lesser officials.)

Rem not only approved of his father's choice of name, he too chose the security service as a career. At a social gathering organised by his department in the KGB Rem was attracted to a girl whose name turned out to be Ninel, Lenin spelt backwards. For the young couple, who quickly married, it must have seemed confirmation that destiny was shaping their lives, a belief deeply held by many Russians, whether or not Pushkin's fatalistic poetry was on the Soviet reading list.

Mr Krasilnikov was given his first glimpse of the world beyond Russia when he was posted to the Russian embassy in Ottawa. Canada provided Russia with a base to view the whole of North America. The embassy had been embarrassed in 1945 when Igor Gouzenko, one of its clerks, had defected with a pile of documents showing that Russia was running a spy operation under diplomatic cover. But Canada took the view that it had few military secrets, and accepted Russia's formal apology and promise not to misbehave again. Counter-intelligence was left to the Mounties, famous for their horses. Mr Krasilnikov travelled freely in the United States. In his biography he says he developed an admiration for Americans. He commended the careful way that the CIA had set up a spy network in the Soviet Union during the cold war, a network that Mr Krasilnikov was to destroy.

Greed and loyalty

Stalin occasionally expressed unease that his spies provided him with a constant flow of the West's most important secrets, such as the development of the atomic bomb. If there were people in America and Britain willing to betray their countries, surely there were traitors in Russia sending information to the enemy? His acolytes sought to assure him that all Russians so loved Stalin that none would betray him. Stalin was unconvinced. His experience told him that human weaknesses, such as misplaced loyalties and simple greed, weakened the state, whatever its ideology. Stalin died in 1953, but his worries were shared by his successors and turned out to be well founded. The round-up and crushing of the West's spy network in Russia was mainly done in the 1980s. By then Rem Krasilnikov had become head of the KGB department dealing with American activities in Moscow, and had the rank of major-general.

Three Americans, Edward Lee Howard and Aldrich Ames, both employed by the CIA, and Robert Hanssen, an FBI employee, turned out to be working for the Russians. At the trials of Mr Ames and Mr Hanssen it was disclosed they had been paid hundreds of thousands of dollars. Mr Howard escaped to Russia. All three men had provided Mr Krasilnikov with lists of Russians who were supplying the West with information. Perhaps the most important was Adolf Tolkachev, a scientist who had sent information to the Americans that helped them to make their stealth aircraft and achieve superiority over anything flying.

Mr Krasilnikov's team arrested everyone on the lists, but initially kept the arrests secret. Anyone who tried to contact any of those held would themselves be arrested. If the contacts were merely diplomats they were deported. Otherwise they would be questioned, given a formal trial and executed. By the end

of the 1980s Mr Krasilnikov could claim that not a single CIA spy existed in the Soviet Union. It was an extraordinary coup. Mr Krasilnikov said the lists provided by the three Americans had helped, but its completeness was due to his tenacity.

In 1991 the Soviet Union broke up. Mr Krasilnikov retired in 1992. He predicted, reasonably, that spying would continue. “Russia will certainly not give it up,” he said. Spying is continuing between India and Pakistan, between the two Koreas, between Taiwan and China, between Israel and its neighbours, and so on. But spying as a career may have been downgraded now that there are no longer two superpowers seeking out each other's deadly secrets in the struggle for world domination. Thriller writers, at least, are having to find new territory.

Rem and Ninel had a son and a daughter. In the 1950s, when they were born, the revolution had long lost its romantic lustre, and traditional names had returned to favour even among officials. They called them Sergei and Tatiana.

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Overview

Apr 3rd 2003
From The Economist print edition

America's economy is still losing steam: the Institute for Supply Management's (ISM) manufacturing index recorded a sharp fall in March to 46.2, down from 50.5 in February. March's reading points to shrinking factory output, which analysts put down to uncertainty caused by the war with Iraq. Even so, the fall in the ISM index since the beginning of 2003 is the largest in any three-month period since the early 1980s.

The latest consumer-confidence figures from the University of Michigan also suggest deepening gloom: its index fell to 77.6 in March, from 79.9 in February.

In the 12 months to February, American retail sales rose by 2.1% in volume, following a more robust rise of 5.0% in the 12 months to January.

Europe's sluggish economic growth is taking a toll on employment. Euro-area unemployment rose from 8.6% in January to 8.7% in February. France's unemployment rose to 9.2% in February, from 9.1% in January. Italy's unemployment also rose, from 8.9% in December to 9.0% in January.

In **Japan**, however, the employment situation improved. Unemployment fell from 5.5% in January to 5.2% in February.

Workers in **Canada** received a 1.8% pay rise in the year to January, a real cut of 2.6%.

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Output, demand and jobs

Apr 3rd 2003
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2003	2004	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 3.0	Q4	+ 1.6	+ 3.0	+ 3.6	+ 2.3	Q4	+ 5.4	Q4	6.0	Feb	6.6
Austria	+ 1.2	Q3	+ 0.3	+ 1.0	+ 1.9	− 1.5	Dec	+ 0.9	Dec	4.3	Mar	4.0
Belgium	+ 1.6	Q4	+ 0.8	+ 1.2	+ 2.2	+ 3.3	Jan	+ 3.5	Jan	11.7	Mar†	10.8
Britain	+ 2.2	Q4	+ 1.7	+ 1.9	+ 2.5	− 0.7	Jan	+ 3.2	Feb	5.0	Jan††	5.1
Canada	+ 3.9	Q4	+ 1.6	+ 2.8	+ 3.3	+ 4.2	Jan	+ 1.4	Dec	7.4	Feb	7.9
Denmark	+ 0.9	Q4	− 0.1	+ 1.5	+ 2.3	− 1.7	Dec	+ 2.4	Dec	5.7	Feb	5.0
France	+ 1.7	Q4	+ 0.9	+ 1.2	+ 2.3	+ 1.0	Jan	− 1.9	Dec	9.2	Feb	8.8
Germany	+ 0.5	Q4	− 0.1	+ 0.4	+ 1.6	− 0.2	Jan	+ 0.4	Feb	10.6	Mar§	9.6
Italy	+ 1.0	Q4	+ 1.7	+ 1.0	+ 2.0	− 1.5	Jan	+ 1.9	Nov†	9.0	Jan	9.0
Japan	+ 2.8	Q4	+ 2.2	+ 0.7	+ 0.8	+ 4.2	Feb	− 2.4	Jan	5.2	Feb	5.3
Netherlands	+ 0.3	Q4	+ 0.4	+ 0.6	+ 1.9	− 2.3	Jan	− 2.5	Dec	4.6	Feb†**	3.7
Spain	+ 2.1	Q4	+ 1.4	+ 2.1	+ 2.7	+ 2.5	Dec	+ 2.5	Jan	11.9	Feb	11.1
Sweden	+ 1.3	Q4	+ 1.2	+ 1.7	+ 2.4	+ 3.7	Jan	+ 4.2	Feb	4.5	Feb†	4.0
Switzerland	+ 0.8	Q4	+ 1.4	+ 0.8	+ 1.8	− 2.1	Q4	− 2.8	Dec	3.9	Feb†	2.6
United States	+ 2.9	Q4	+ 1.4	+ 2.2	+ 3.3	+ 1.8	Feb	+ 2.1	Feb	5.8	Feb	5.6
Euro area	+ 1.3	Q4	+ 0.7	+ 1.0	+ 2.1	+ 0.7	Jan	+ 2.7	Jan	8.7	Feb	8.1
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 2.8	Q4	+ 2.8	na	na	+ 3.6	Feb	+ 2.0	Nov	9.0	Feb†	9.4
Greece	+ 3.5	Q4	na	na	na	− 0.3	Jan	na		na		na
Iceland	− 3.0	Q4	na	na	na	+12.2	2001	na		4.1	Feb†	2.6
Ireland	+ 6.9	Q3	na	na	na	+ 5.4	Jan	+ 4.7	Jan	4.5	Feb†	4.3
Luxembourg	+ 1.0	2001	na	na	na	+ 3.6	Dec	− 6.1	Oct	3.8	Feb†	2.9
New Zealand	+ 4.2	Q4	+ 2.0	na	na	+ 5.1	Q3	+ 7.3	Q4	4.9	Q4	5.4
Norway	− 0.1	Q4	+ 0.9	na	na	− 4.6	Jan	+ 3.1	Feb	3.7	Q4	3.3
Portugal	− 1.3	Q4	− 3.1	na	na	+ 3.4	Feb	+ 2.3	Feb	6.2	Q4†	4.2

*% change at an annual rate. †Not seasonally adjusted. ‡New series. ††Nov-Jan; claimant count rate 3.1% in Feb. §EU harmonised rate 8.9% in March. **Dec-Feb, new series.

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Prices and wages

Apr 3rd 2003
From The Economist print edition

% change on year ago

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2003	2004	latest		year ago	latest		year ago
Australia	+ 3.0	Q4	+ 3.1	+ 2.7	+ 2.5	+ 1.6	Q4	– 0.7	+ 3.9	Q4	+ 4.9
Austria	+ 1.7	Feb	+ 1.9	+ 1.7	+ 1.3	+ 2.1	Feb	– 0.6	+ 2.2	Feb	+ 2.5
Belgium	+ 1.8	Mar	+ 2.7	+ 1.5	+ 1.4	+ 0.3	Feb	– 0.6	+ 2.2	Q4	+ 3.1
Britain	+ 3.2	Feb	+ 1.0	+ 2.8	+ 2.5	+ 1.6	Feb	– 0.2	+ 3.6	Jan	+ 3.0
Canada	+ 4.6	Feb	+ 1.5	+ 3.0	+ 2.2	+ 2.3	Feb	– 1.1	+ 1.8	Jan	+ 3.7
Denmark	+ 2.9	Feb	+ 2.5	+ 2.3	+ 2.0	+ 1.7	Feb	nil	+ 3.9	Q4	+ 4.1
France	+ 2.6	Feb	+ 2.0	+ 1.7	+ 1.4	+ 2.8	Feb	– 1.4	+ 3.5	Q4	+ 3.9
Germany	+ 1.2	Mar	+ 2.0	+ 1.1	+ 1.0	+ 1.6	Feb	– 0.5	+ 2.6	Jan	+ 2.3
Italy	+ 2.7	Mar	+ 2.5	+ 2.3	+ 1.9	+ 2.8	Feb	– 1.1	+ 2.1	Dec	+ 2.8
Japan	– 0.2	Feb	– 1.6	– 0.6	– 0.5	– 0.9	Feb	– 2.6	+ 2.1	Feb	– 0.6
Netherlands	+ 2.7	Mar	+ 3.7	+ 2.6	+ 2.1	+ 5.1	Feb	– 2.6	+ 3.0	Feb	+ 4.4
Spain	+ 3.8	Feb	+ 3.1	+ 3.0	+ 2.6	+ 2.9	Feb	– 0.2	+ 3.9	Q4	+ 3.7
Sweden	+ 3.4	Feb	+ 2.8	+ 2.4	+ 2.0	+ 0.6	Feb	– 0.4	+ 4.0	Dec	+ 3.2
Switzerland	+ 1.3	Mar	+ 0.6	+ 0.7	+ 0.9	nil	Feb	– 1.5	+ 2.5	2001	+ 1.3
United States	+ 3.0	Feb	+ 1.1	+ 2.3	+ 1.8	+ 3.5	Feb	– 2.6	+ 3.2	Feb	+ 3.5
Euro area	+ 2.4	Mar	+ 2.5	+ 1.8	+ 1.5	+ 2.0	Jan	– 0.8	+ 3.4	Q4	+ 3.2
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 1.9	Feb	+ 1.8	na	na	+ 2.3	Feb	– 1.4	+ 3.3	Q4	+ 4.5
Greece	+ 4.3	Feb	+ 3.4	na	na	+ 2.7	Feb	+ 3.5	na		na
Iceland	+ 2.2	Mar	+ 8.7	na	na	+ 3.3	Apr	+ 8.7	+ 5.6	Feb	+ 9.8
Ireland	+ 5.1	Feb	+ 4.7	na	na	– 5.3	Jan	+ 1.7	+ 6.8	Q4	+ 7.8
Luxembourg	+ 2.5	Feb	+ 2.3	na	na	+ 1.3	Jan	– 2.0	+ 0.5	Dec	nil
New Zealand	+ 2.7	Q4	+ 1.8	na	na	– 0.9	Q4	+ 1.8	+ 2.1	Q4	+ 2.2
Norway	+ 4.8	Feb	+ 0.8	na	na	+11.9	Feb	–11.5	+ 5.2	Q4	+ 4.4
Portugal	+ 4.2	Feb	+ 3.2	na	na	+ 2.7	Feb	– 0.6	+ 0.4	Jan*	+ 1.3

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Economic forecasts

Apr 3rd 2003
From The Economist print edition

Every month *The Economist* surveys a group of forecasters and calculates the average of their predictions for economic growth, inflation and current-account balances for 15 countries and for the euro area. The table also shows the highest and lowest projections for growth. The previous month's forecasts, where different, are shown in brackets. This month the panel has become more pessimistic about the outlook for growth in almost all countries. It now expects the United States to grow by 2.2% in 2003, down from 2.5% a month ago; and by 3.3% in 2004, down from 3.5%. The growth forecast for the euro area has also been pared for both years. Britain is now predicted to grow by 1.9% in 2003, down from 2.2% in March; and by 2.5% in 2004, down from 2.7%. However, the panel thinks that Japan will do a little better in both years.

The Economist poll of forecasters, April averages (previous month's, if changed)

	Real GDP, % change Low/high range		Real GDP, % change average		Consumer prices % increase		Current account % of GDP	
	2003	2004	2003	2004	2003	2004	2003	2004
Australia	2.7/3.6	3.0/4.4	3.0 (3.1)	3.6 (3.4)	2.7	2.5 (2.9)	–4.7(–4.3)	–3.9 (–3.8)
Austria	0.5/1.7	1.5/2.3	1.0 (1.2)	1.9 (2.0)	1.7	1.3 (1.5)	–0.7	–0.9 (–1.4)
Belgium	0.6/1.8	1.8/2.4	1.2 (1.3)	2.2 (2.3)	1.5 (1.3)	1.4 (1.5)	4.9	4.9 (5.0)
Britain	1.4/2.4	1.5/3.3	1.9 (2.2)	2.5 (2.7)	2.8 (2.6)	2.5 (2.5)	–1.8(–1.9)	–1.6 (–1.8)
Canada	2.3/3.4	2.7/4.0	2.8 (3.0)	3.3	3.0 (2.8)	2.2 (2.3)	1.6 (1.9)	1.7 (2.0)
Denmark	1.0/2.2	1.9/2.5	1.5 (1.8)	2.3 (2.4)	2.3 (2.1)	2.0 (1.9)	2.0 (2.0)	1.9 (1.7)
France	0.9/1.5	1.7/3.4	1.2 (1.4)	2.3 (2.4)	1.7 (1.5)	1.4	1.7	1.6 (1.5)
Germany	–0.1/0.7	1.1/2.2	0.4 (0.5)	1.6 (1.9)	1.1 (1.0)	1.0 (1.1)	1.9 (1.7)	1.8 (1.5)
Italy	0.4/1.6	1.3/2.7	1.0 (1.2)	2.0 (2.2)	2.3	1.9 (2.0)	–0.4(–0.2)	–0.3 (–0.1)
Japan	0.0/1.7	0.0/2.0	0.7 (0.5)	0.8 (0.6)	–0.6	–0.5	2.6 (2.7)	2.9 (2.9)
Netherlands	–0.2/1.1	1.4/2.9	0.6 (0.8)	1.9 (2.2)	2.6 (2.5)	2.1 (2.2)	3.2 (3.1)	3.2 (3.2)
Spain	1.7/2.5	2.2/3.3	2.1 (2.2)	2.7 (2.9)	3.0 (3.0)	2.6 (2.7)	–2.2(–2.0)	–2.1 (–2.0)
Sweden	1.4/2.1	2.2/2.9	1.7 (1.9)	2.4 (2.5)	2.4 (2.2)	2.0 (2.1)	3.6 (3.3)	3.5 (3.3)
Switzerland	0.5/1.2	1.0/2.4	0.8 (0.9)	1.8 (1.9)	0.7	0.9 (1.0)	11.2(10.8)	11.4 (11.6)
United States	1.7/2.8	2.0/4.5	2.2 (2.5)	3.3 (3.5)	2.3 (2.2)	1.8 (1.9)	–5.4(–5.1)	–5.3 (–4.0)
Euro area	0.6/1.5	1.7/2.7	1.0 (1.1)	2.1 (2.2)	1.8 (1.7)	1.5 (1.6)	0.8 (0.9)	0.8

Sources: ABN Amro, Deutsche Bank, Economist Intelligence Unit, Goldman Sachs, HSBC Securities, KBC Bank, Merrill Lynch, J.P. Morgan Chase, Morgan Stanley, Nordea, Decision Economics, BNP Paribas, Royal Bank of Canada, Schroder Salomon Smith Barney, Scotiabank, UBS Warburg

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Money and interest rates

Apr 3rd 2003
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Apr 2nd 2003)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	−11.8	+10.3	Feb	4.79	4.55	4.60	5.38	6.38	6.47
Britain	+ 6.2	+ 6.7	Feb	3.59	4.19	3.42	4.38	5.22	6.03
Canada	+ 5.7	+ 3.7	Feb	3.17	2.22	3.92	5.23	5.72	7.06
Denmark	+ 8.7	+10.4	Feb	2.70	3.75	2.69	4.31	5.36	5.46§
Japan	+21.3	+ 2.0	Feb	0.02	0.03	0.05	0.70	1.40	0.81
Sweden	+ 0.4	+ 5.2	Jan	3.38	4.19	3.55	4.58	5.57	4.06
Switzerland	+12.9	+ 8.7	Feb	0.31	1.61	0.42	2.38	3.49	3.18
United States	+ 3.8	+ 6.3	Feb	1.17	1.89	1.59	3.93	5.28	5.99
Euro area†	+10.3	+ 8.1	Feb	2.51	3.44	2.45	4.06	5.13	4.51

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. §New series. Benchmarks: US 30-year 4.93%, Japan No.247 0.70%. Central bank rates: US fed funds 1.25%, ECB refinancing 2.50%, BOJ overnight call 0.001%, BOE repo 3.75%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS Warburg, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Apr 3rd 2003
From The Economist print edition

1995=100

	Mar 25th	Apr 1st*	% change on one month	% change on one year
Dollar index				
All items	75.8	75.0	– 4.4	+ 6.8
Food	76.4	76.7	– 3.6	+ 8.6
Industrials				
All	74.9	72.7	– 5.6	+ 4.2
Nfa†	78.3	76.9	– 3.7	+11.1
Metals	72.1	69.2	– 7.3	– 1.6
Sterling index				
All items	76.1	75.2	– 3.9	– 2.2
Euro index				
All items	93.2	90.5	– 4.4	–13.7
Yen index				
All items	96.7	94.4	– 4.1	– 5.3
Gold				
$ per oz	329.80	335.00	– 5.2	+ 9.7
West Texas Intermediate				
$ per barrel	27.95	29.75	–19.4	+ 8.5

* Provisional. † Non-food agriculturals.

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Stockmarkets

Apr 3rd 2003
From The Economist print edition

Market indices

	Apr 2nd	2003 high	2003 low	% change on one week	% change on record high	% change on Dec 31st 2002 in local currency	% change on Dec 31st 2002 in $ terms
Australia (All Ordinaries)	2,847.4	3,049.6	2,673.3	– 0.4	–17.2	– 4.3	+ 2.1
Austria (ATX)	1,186.8	1,187.8	1,120.2	+ 1.3	–31.7	+ 3.2	+ 6.1
Belgium (Bel 20)	1,718.2	2,074.1	1,426.6	– 0.1	–53.3	–15.2	–12.8
Britain (FTSE 100)	3,753.4	4,009.5	3,287.0	– 1.0	–45.8	– 4.7	– 7.1
Canada (Toronto Composite)	6,411.2	6,837.3	6,228.6	+ 0.9	–43.7	– 3.1	+ 3.6
Denmark (KBX)	164.0	173.2	145.0	+ 1.4	–45.7	– 1.4	+ 1.4
France (SBF 250)	1,836.6	2,144.8	1,630.1	– 1.6	–58.2	–10.6	– 8.0
(CAC 40)	2,743.9	3,210.3	2,403.0	– 1.6	–60.4	–10.4	– 7.9
Germany (DAX)	2,589.4	3,157.3	2,203.0	+ 0.4	–67.9	–10.5	– 8.0
Italy (BCI)	1,038.0	1,142.4	959.4	– 0.9	–52.4	– 4.9	– 2.3
Japan (Nikkei 225)	8,069.9	8,790.9	7,862.4	– 3.4	–79.3	– 5.9	– 6.2
(Topix)	797.6	865.4	760.1	– 2.9	–72.4	– 5.4	– 5.7
Netherlands (AEX)	265.2	337.3	218.4	– 0.5	–62.2	–17.8	–15.5
Spain (Madrid SE)	641.5	683.8	576.8	+ 0.3	–44.0	+ 1.2	+ 4.0
Sweden (Affarsvarlden Gen)	139.8	153.4	127.8	– 1.2	–65.1	– 3.7	– 1.9
Switzerland (Swiss Market)	4,272.1	4,965.3	3,675.4	+ 0.6	–49.2	– 7.7	– 7.2
United States (DJIA)	8,285.1	8,842.6	7,524.1	+ 0.7	–29.3	– 0.7	– 0.7
(S&P 500)	880.9	931.7	800.7	+ 1.3	–42.3	+ 0.1	+ 0.1
(NASDAQ Comp)	1,396.7	1,461.0	1,271.5	+ 0.7	–72.3	+ 4.6	+ 4.6
Europe (FTSE Eurotop 300)*	778.9	890.8	682.7	– 1.2	–54.3	– 9.1	– 6.5
Euro area (FTSE Ebloc 100)*	651.7	757.2	565.7	– 0.6	–58.0	– 9.3	– 6.7
World (MSCI)†	773.2	830.7	710.8	+ 0.4	–46.6	na	– 2.4
World bond market (Salomon)‡	536.6	551.7	518.6	+ 1.0	– 2.7	na	+ 2.1

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms.
‡Salomon Smith Barney World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Apr 3rd 2003
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current account $bn latest 12 mths		The Economist poll % of GDP, forecast 2003	2004	Exchange rate trade-weighted† 1990=100 Apr 2nd	year ago	Currency units per $ Apr 2nd	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2002‡
Australia	− 6.7	Feb	− 17.7	Q4	− 4.7	− 3.9	77.2	76.1	1.67	1.88	2.61	1.80	1.40	0.1
Austria	+ 0.4	Dec	+ 0.9	Jan	− 0.7	− 0.9	101.7§	100.3	0.93	1.14	1.45	–	0.78	-1.6
Belgium	+ 16.4	Jan	+ 12.8	Sep	+ 4.9	+ 4.9	101.4§	99.0	0.93	1.14	1.45	–	0.78	nil
Britain	− 53.6	Jan	− 13.1	Q4	− 1.8	− 1.6	99.9	107.3	0.64	0.70	–	0.69	0.54	-1.4
Canada	+ 34.7	Jan	+ 11.0	Q4	+ 1.6	+ 1.7	79.6	76.0	1.48	1.59	2.32	1.60	1.24	0.6
Denmark	+ 8.1	Jan	+ 5.1	Jan	+ 2.0	+ 1.9	105.4	101.7	6.88	8.44	10.8	7.43	5.78	2.2
France	+ 9.0	Jan	+ 27.3	Jan	+ 1.7	+ 1.6	104.5§	101.6	0.93	1.14	1.45	–	0.78	-2.7
Germany	+120.0	Jan	+ 48.3	Jan	+ 1.9	+ 1.8	101.8§	98.5	0.93	1.14	1.45	–	0.78	-3.7
Italy	+ 8.2	Jan	− 8.8	Jan	− 0.4	− 0.3	74.5§	72.5	0.93	1.14	1.45	–	0.78	-2.3
Japan	+ 93.6	Jan	+113.4	Jan	+ 2.6	+ 2.9	131.1	127.6	119	133	187	128	–	-7.9
Netherlands	+ 29.1	Jan	+ 9.1	Q4	+ 3.2	+ 3.2	100.7§	97.9	0.93	1.14	1.45	–	0.78	-0.8
Spain	− 40.8	Jan	− 17.1	Dec	− 2.2	− 2.1	76.0§	74.2	0.93	1.14	1.45	–	0.78	nil
Sweden	+ 15.0	Feb	+ 9.9	Dec	+ 3.6	+ 3.5	78.9	76.8	8.55	10.3	13.4	9.23	7.19	1.7
Switzerland	+ 4.7	Feb	+ 32.0	Q4	+11.2	+11.4	115.4	112.8	1.37	1.66	2.16	1.48	1.16	na
United States	−495.8	Jan	−503.4	Q4	− 5.4	− 5.3	108.0	123.0	–	–	1.57	1.08	0.84	-3.1
Euro area	+ 95.5	Jan	+ 53.5	Jan	+ 0.8	+ 0.8	87.2	78.3	0.93	1.14	1.45	–	0.78	-2.2
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 13.5	Jan	+ 10.5	Jan	na	na	80.4§	78.2	0.94	1.14	1.48	–	0.79	3.2
Greece	− 22.0	Jan	− 10.1	Jan	na	na	58.7§	57.5	0.94	1.14	1.48	–	0.79	-1.1
Iceland	+ 0.2	Feb	nil	Q4	na	na	93.0**	80.4	77.5	99.3	122	83.6	65.1	0.3
Ireland	+ 36.1	Jan	+ 0.1	Q3	na	na	91.6§	87.2	0.94	1.14	1.48	–	0.79	-0.5
Luxembourg	− 3.1	Dec	+ 1.7	Q4	na	na	101.4§	99.0	0.94	1.14	1.48	–	0.79	1.8
New Zealand	− 0.9	Feb	− 1.9	Q4	na	na	96.7	85.2	1.81	2.28	2.84	1.95	1.52	1.6
Norway	+ 28.0	Feb	+ 27.4	Jan	na	na	101.8	99.7	7.25	8.69	11.4	7.82	6.09	12.4
Portugal	− 12.8	Dec	− 9.2	Jan	na	na	91.3**	89.9	0.94	1.14	1.48	–	0.79	-3.4

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, January average. ‡OECD estimate. **IMF, November average.

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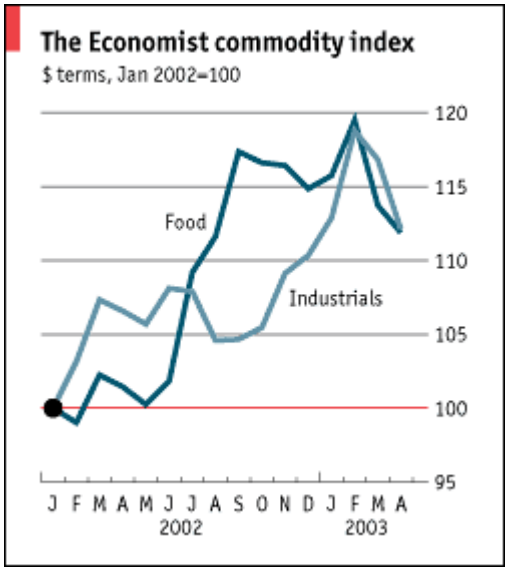
The Economist commodity index

Apr 3rd 2003
From The Economist print edition

After more than a year of rising prices, *The Economist*'s food and industrial indices have declined. Since mid-February, cocoa and sugar prices have fallen by 15% apiece, and nickel by 9%.



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Overview

Apr 3rd 2003
From The Economist print edition

The economic outlook for some Asian economies, particularly **Hong Kong**, is darkening, as fears mount over the effects of SARS (severe acute respiratory syndrome). Higher oil prices are worsening **South Korea's** trade balance and boosting inflation. On a monthly basis, the country ran a trade deficit for the third consecutive month in March. South Korean consumer prices rose by 4.5% in the year to March, up from 3.9% in the year to February.

Singapore's economy, too, shows signs of trouble. Industrial production fell by 1.4% in the year to February, after rising by 13.4% in the year to January.

Turkey's GDP grew by 11.4% in the year to the fourth quarter of 2002, the fastest rate since early 1995. The country's trade deficit widened to $16 billion in the year to January.

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Genetically modified food

Apr 3rd 2003
From The Economist print edition

Countries due to join the European Union in 2004 take a dim view of genetically modified (GM) foods, according to a poll released this week by the European Commission. Its Eurobarometer survey gauged the attitudes of more than 12,000 people in EU candidate countries towards biotechnology. More than 80% of those surveyed thought that science would improve their lives, but 68%, on average, reject GM food, with more than half believing the stuff to be positively dangerous.

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Economy

Apr 3rd 2003
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 8.1	Q4	+19.8	Feb	+ 0.2	Feb	+23.9	Feb	+17.4	2001	269.9	Oct
Hong Kong	+ 5.0	Q4	– 9.2	Q4	– 2.0	Feb	– 7.9	Feb	+13.8	Q4	113.7	Feb
India	+ 2.6	Q4	+ 6.4	Jan	+ 3.4	Jan	– 7.9	Jan	+ 4.5	Q3	69.2	Feb
Indonesia	+ 3.8	Q4	+ 7.1	Dec‡	+ 7.1	Mar	+25.6	Feb	+ 7.5	Q3	31.1	Feb
Malaysia	+ 5.6	Q4	+ 1.0	Jan	+ 1.6	Feb	+14.3	Feb	+ 7.3	Q4	34.5	Feb
Philippines	+ 5.8	Q4	+ 4.9	Jan	+ 3.1	Feb	+ 0.7	Jan	+ 6.1	Sep	13.1	Feb
Singapore	+ 2.7	Q1	– 1.4	Feb	+ 0.4	Feb	+10.7	Feb	+18.7	Q4	83.6	Feb
South Korea	+ 6.8	Q4	+10.2	Feb	+ 4.5	Mar	+ 7.7	Mar	+ 5.1	Feb	123.9	Feb
Taiwan	+ 4.2	Q4	+10.1	Feb	– 1.5	Feb	+16.2	Feb	+25.8	Q4	166.3	Feb
Thailand	+ 6.1	Q4	+12.8	Feb	+ 1.7	Mar	+ 4.8	Feb	+ 8.3	Feb	38.9	Jan
Argentina	– 3.6	Q4	+12.3	Feb	+36.1	Feb	+15.9	Jan	+ 8.9	Q4	10.3	Feb
Brazil	+ 3.4	Q4	+ 2.8	Jan	+15.9	Feb	+16.0	Mar	– 5.5	Feb	38.6	Jan
Chile	+ 3.2	Q4	+ 7.8	Feb	+ 3.8	Feb	+ 2.3	Feb	– 0.6	Q4	16.5	Feb
Colombia	+ 2.0	Q4	+ 5.6	Dec	+ 7.2	Feb	nil	Dec	– 1.5	Q3	10.9	Feb
Mexico	+ 1.9	Q4	+ 0.3	Jan	+ 5.5	Feb	– 6.9	Feb	–14.5	Q4	51.5	Jan
Peru	+ 4.6	Jan	+ 4.0	Jan	+ 2.8	Feb	+ 0.3	Jan	– 1.1	Q4	9.3	Jan
Venezuela	–16.7	Q4	–64.8	Dec	+38.7	Feb	+13.9	Q4	+ 7.6	Q4	8.6	Dec
Egypt	+ 3.1	2002†	+ 4.2	2002†	+ 3.0	Dec	– 7.8	Dec	+ 0.5	Q4	13.2	Dec
Israel	+ 1.3	Q4	+ 1.3	Dec	+ 5.1	Feb	– 5.5	Feb	– 2.1	Q4	23.4	Feb
South Africa	+ 3.0	Q4	+ 1.5	Jan	+12.5	Feb	+ 3.9	Feb	+ 0.3	Q4	6.1	Feb
Turkey	+11.4	Q4	+13.2	Jan	+27.0	Feb	–16.0	Jan	– 1.3	Dec	29.2	Jan
Czech Republic	+ 1.5	Q4	+ 6.4	Jan	– 0.4	Feb	– 2.5	Feb	– 3.5	Q4	24.4	Feb
Hungary	+ 3.7	Q4	+ 4.7	Jan	+ 4.5	Feb	– 3.3	Jan	– 2.7	Jan	13.0	Feb
Poland	+ 2.1	Q4	+ 4.1	Feb	+ 0.5	Feb	–10.2	Feb	– 6.5	Jan	30.7	Feb
Russia	+ 4.3	Q3	+ 6.5	Feb	+14.8	Feb	+48.2	Jan	+38.3	Q1	49.3	Feb
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Pakistan	+ 3.6	2002†	+15.8	Nov	+ 3.5	Feb	– 1.4	Feb	+ 2.7	2002†	8.5	Jan
Saudi Arabia	+ 1.2	2001	na		– 0.7	Nov	+39.2	2001	+ 9.4	2001	21.2	Jan

*Excluding gold, except Singapore; IMF definition. †Year ending June. ‡New series.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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Financial markets

Apr 3rd 2003
From The Economist print edition

	Currency units per $ Apr 2nd	Currency units per $ year ago	Currency units per £ Apr 2nd	Interest rates short-term % p.a.	Stockmarkets Apr 2nd	% change on one week	% change on Dec 31st 2002 in local currency	% change on Dec 31st 2002 in $ terms
China	8.28	8.28	13.0	na	1,591.3	+4.5	+ 12.1	+ 12.1
Hong Kong	7.80	7.80	12.2	1.38	8,706.2	-3.8	- 6.6	- 6.6
India	47.4	48.9	74.3	5.89	3,117.0	-0.8	- 7.7	- 6.5
Indonesia	8,884	9,803	13,942	12.11	398.1§	-0.7	- 6.3	- 5.6
Malaysia	3.80	3.80	5.96	3.10	629.0	-0.6	- 2.7	- 2.7
Philippines	53.2	51.2	83.5	9.56	1,052.0	+2.3	+ 3.3	+ 3.6
Singapore	1.77	1.84	2.78	0.75	1,299.8	-1.9	- 3.1	- 5.1
South Korea	1,255	1,324	1,969	4.70	542.9	-2.1	- 13.5	- 18.2
Taiwan	34.8	35.0	54.5	1.40	4,311.6	-4.1	- 3.2	- 3.1
Thailand	43.0	43.7	67.4	1.75	363.0	-1.4	+ 1.8	+ 2.2
Argentina	2.93	2.94	4.59	8.60	561.6	-1.2	+ 7.0	+ 22.9
Brazil	3.27	2.29	5.14	26.33	11,872.0	+5.9	+ 5.4	+ 14.0
Chile	720	657	1,130	2.52	5,065.3	+0.6	+ 0.9	+ 0.9
Colombia	2,958	2,265	4,641	7.80	1,593.5	-0.8	- 0.9	- 4.0
Mexico	10.66	9.04	16.7	8.72	6,008.5	+0.9	- 1.9	- 3.8
Peru	3.47	3.45	5.45	3.94	1,587.4	+2.0	+ 14.0	+ 15.5
Venezuela	1,598	906	2,508	28.62	8,593.7	+2.0	+ 7.2	- 7.0
Egypt	5.76	4.64	9.04	13.59	6,495.7	+7.3	+ 20.9	- 2.8
Israel	4.67	4.78	7.32	6.03	357.6	+1.7	+ 7.6	+ 9.5
South Africa	8.0	11.1	12.5	13.55	7,915.6	+1.0	- 14.7	- 8.0
Turkey	1,684,000	1,320,000	2,642,701	42.00	9,804.9	+4.2	- 5.4	- 6.8
Czech Republic	29.7	34.5	46.6	2.42	500.6	+2.1	+ 8.7	+ 10.0
Hungary	229	276	360	6.55	7,597.1	+0.4	- 2.6	- 4.4
Poland	4.07	4.10	6.38	5.97	13,910.3	-0.9	- 3.2	- 8.7
Russia	31.3	31.2	49.1	18.00	363.2‡	-0.4	- 1.0	+ 1.2
EMF (MSCI)*	1.00	1.00	1.57	na	276.2	-0.9	na	- 5.5
EMBI+†	1.00	1.00	1.57	na	249.3	+2.0	na	+ 8.9

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡ In $ terms. §Apr 1st

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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